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STUDIES IN TAXATION

NORTH CAROLINA CLUB YEARBOOK
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Taxes are simply one-sided transfers of economic goods or services demanded of the citizens, and occasionally of those not citizens, but who, nevertheless, are within the reach of the taxing power, by the constituted authorities of the land, for meeting the expenses of government, or for some other purpose, with the intention that a common burden shall be maintained by common contributions or sacrifices.

—Richard T. Ely.

A man is taxed not to pay the state for its expense in protecting him, and not in any respect as a recompense to the state for any service in his behalf, but because his original relations to society require it. All the enjoyments which a man can receive from his property come from his connection with society. Cut off from all social relations a man's wealth would be useless to him. In fact, there would be no such thing as wealth without society. Wealth is what may be exchanged, and requires for its existence a community of persons with reciprocal wants.... It is wise and right, therefore, for an individual to contribute of his wealth what the true interests of society require, and this he does, not as a payment for the gifts which society has conferred.*—Report of Massachusetts Tax Commissioners, 1875.*

I have never viewed taxation as a means of rewarding one class of taxpayers or punishing another. If such a point of view ever controls our public policy, the traditions of freedom, justice and equality of opportunity, which are the distinguishing characteristics of our American civilization, will have disappeared and in their place we shall have class legislation with all its attendant evils.

—Andrew W. Mellon.

Amid the clashing of divergent interests, and the endeavor of each social class to roll off the burden of taxation on some other class, we discern the slow and laborious growth of standards of justice in taxation, and the attempt on the part of the community as a whole to realize this justice.

—Edwin R. A. Seligman.

THE NORTH CAROLINA CLUB 1927-1928

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FOREWORD

PAUL W. WAGER

The North Carolina Club is composed of those students and faculty members at the state university who are interested in building on the soil of North Carolina a great commonwealth. It is composed of those, or some of those, whose interest extends beyond the borders of the campus into the realm of public affairs—or in other words, to the civic, social, and economic problems with which the state is wrestling.

The Club was organized in 1914 by Dr. E. C. Branson, who is still its guiding spirit and most faithful attendant. He believes that a proper study for North Carolinians is North Carolina, its resources and short-comings, its opportunities and its tasks. He believes that it is the function of a state university to acquaint its students with state problems, give them experience in analysis and research, and equip them with the technique and the vision for constructive leadership. The North Carolina Club exists primarily to help in the performance of this function.

Each year the Club concentrates its attention on a series of related topics, the program of the year usually consisting of some fifteen fortnightly sessions. In addition to reports by student investigators, the club program includes a few addresses by people prominent in the life of the state.

Each year the papers read before the North Carolina Club are assembled into a yearbook. The yearbooks to date are:

1915-1916	The Resources, Advantages, and Opportunities of North Carolina
1916-1917	Wealth and Welfare in North Carolina
1917-1918	County Government and County Affairs in North Carolina
1918-1919	No yearbook issued
1919-1920	State Reconstruction Studies
1920-1921	North Carolina, Urban and Industrial
1921-1922	Home and Farm Ownership
1922-1923	What Next in North Carolina? I
1923-1924	What Next in North Carolina? II
1924-1925	What Next in North Carolina? III
1925-1926	Town and Country Interdependencies
1926-1927	Some Problems in Democracy in North Carolina

Probably the most discussed topic in the state now is taxation. For this reason the Club gave its attention this year to an examination of our tax system. The yearbook includes two studies that were made for the Tax Commission; all the others are papers prepared for or delivered to the North Carolina Club in substantially their present form.

THE J. W. BAILEY AWARD

Hon. J. W. Bailey, of Raleigh, offers annually a prize of fifty dollars in gold to that member of the Club who makes the "most valuable contribution of information affecting our Commonwealth." The award for the past college year was won by Mr. S. M. Derrick, of South Carolina, whose paper entitled "Consumption Excise Taxes for State Purposes," was adjudged the best.

THE HISTORICAL BACKGROUND OF THE TAX QUESTION

Robert B. House, *University of North Carolina*

I am glad to be back with the North Carolina Club. I was a charter member. My first appearance on the program was in a debate on the dog tax in 1914, and I have been thinking about taxation ever since. I am voicing, therefore, some ideas that I have been mulling over in my head as I have read history in general and the history of North Carolina in particular.

I should like to explain at first my purpose in taking as a topic "The Historical Background of the *Tax Question.*" There is, of course, a history of taxation development that is technical and self-contained, a chapter of formal economic history. But someone else ought to present this story, for I am not possessed of sufficient technical training to make it clear. My emphasis is on the words, *tax question.* Few men may really know the ins and outs of taxation as a science; but all men feel and think about it. I shall try to bring up some of these attitudes, which, whether they are correct or not, are real and powerful elements in the minds of our people.

We of course want to know the pertinent facts fully and comprehensively. We want to marshal this information and review it scientifically and impartially. And we want to draw conclusions about taxation and form plans that will be just and effective. But taxation is a public question; action about it is authoritative only by public consent. Our conclusions and plans, therefore, must be of a nature that coincides with public opinion. In fact, the problem of just taxation is one primarily of enlightened and just public opinion. We might define taxation under the theory of popular government as the investment by the people of a just proportion of their common wealth in their common welfare. Viewed thus simply, the problem would reduce itself to a clear visioning of the objects of public welfare, accurate measuring of public resources, and scientific means of determining the proportion of wealth thus to be invested. We see clearly enough that this is a field of economics and public finance in which the experts must give us their best judgment. In this group we should perhaps regard the judgment of the expert as an authoritative guide.

But in the larger, human view I doubt if many of us are without bias in thinking of taxation. And I know that as the average citizen thinks of the questions involved he enters at once a field of age-old emotions and prejudices that make scientific thinking practically impossible. It is this average citizen, however, who must be convinced of our knowledge, accuracy, and fairness before he will regard with any confidence what we have to tell him. It is this deposit of historical emotion in our own minds that may obstruct our own vision. And therefore I believe it highly important that we know first of all the historic attitudes of our people toward taxation before we seek to alter them or act in the face of them.

Taxation must have made a bad start in the early days of our race. You will recall Rehoboam and that angry mob who, over two thousand year ago,

had assembled at Shechem to petition for a redress of grievances. There were the oily-tongued old counsellors who said: "Give them a little soft soap. Tell them you will do better by them. They will go home in good humour; then you may do what you please." There were also the rough and ready young fellows of Rehoboam's own mind. They said: "Tell 'em the truth, that this kingdom is your property and you will do what you please with it." One group had learned diplomacy but not honesty. The other had learned honesty without diplomacy. Neither had learned consideration of the common man. Rehoboam followed the counsel of the younger group and precipitated quickly a struggle that wrecked Israel. The rumblings of the maltreated populace that went away from Shechem on that day and of other discontented, tax-ridden mobs echo throughout the whole of ancient history.

INHERITED ATTITUDES

Our own particular folk history takes rise from Rome. In this empire the tax-gatherer was the most hated official. Bernard Shaw says that the power of Julius Caesar was really based on his effectiveness as a tax-collector. In its later days the empire could not find men to discharge this hated duty. Our own word "tax" derives from this time. It comes from *taxare,* to touch rudely, to pry into. The implication is that the man subjected to this was insulted by the process. We get a picture of the rustic glaring at the king's agent who searches through his poor goods and takes the king's share with no regard for the peasant's welfare.

"Imposition" was the name of an arbitrary tax in the time of Charles I. A "monopoly" was also the name of a special arbitrary form of raising money; for instance, the hated salt-tax monopoly of the French, when it was punishable by death to obtain salt except from the authorized agent of the monopoly. Always in the names of these taxes and the connotations of these names in our speech today we catch an idea of the hatefulness of the tax, the conviction of the man taxed that he had to give of his honest toil for the support of a despot—and often a debauched despot. Is it any wonder that these words, monuments as they are to these ancient wrongs, should be remembered with resentment? The attitudes they present are part of our folk inheritance.

As the church began to take over and preserve the governmental system of the empire it also imposed "benefits," "indulgences," and other forms of taxes. It will be remembered that one of Martin Luther's chief grievances against the Pope was his resentment of the "indulgences" by which the Pope sought to raise funds for St. Peter's. Taxation was always an issue in the struggle over church government.

When the national states fought themselves free of the Roman system their governments assumed the form of absolute monarchies in which the king imposed taxes. As the people fought through the centuries for control of their governments taxation was always an issue. The long struggle between king and parliament in England was primarily over who should control the purse of the nation. Is it any wonder, therefore, that the very victories of democracy should have been dramatized in the popular mind as victories over taxation? As more and more people came into the actual business of government, it is

evident that they had to deal with the problems of public revenue and came naturally to see that just taxation imposed on themselves by a self-governing people was one of the necessary functions of government. But self-government has come relatively very late in our Western World. The enlightened student-citizen and statesman type is still relatively small in comparison with the conservative, socially lagging individualist who nurses his grievances against taxation that are older than the whole theory and practice of democracy. Modern social studies reveal large areas of this lagging type of social consciousness. And among the prejudices that characterize this type of citizen in all times and places is that inherent suspicion of taxation.

The colonization and development of America accentuated these prejudices in our social inheritance. In the light of history we know that the British Empire and the proprietors who advanced money for the promotion of colonization had rights and privileges worthy of respect. But our whole colonial history is one of a contest between the individualistic colonists and the prerogative of crown and proprietor. Our forefathers came over here to get a new start under a new system. They were never impressed with respecting the rights of the home government any more than was perfectly convenient to themselves.

Britain operated at that time on the theory of mercantilism, holding that the colonies were right and proper subjects of exploitation by the mother country. They were to submit to rules and regulations made for them in England. Their manufactures and trade were to be restricted for the benefit of the British manufacturers and merchants. Their shipping was to be done in British ships. They were to pay duties as commanded and be taxed as Parliament should decide without consulting them. The colonists never yielded on a single one of these demands. They cheerfully resorted to smuggling, blockade manufacturing, and evasion of the duties and taxes. All through the ages evasion of the taxes had been held as a legitimate protection against unjust measures. The American colonists applied the principle of evasion to all taxes. They asserted their rights, first as Britishers and later as Americans, to control the principles and machinery of taxation. And, finally, they revolted and won their independence on the issue of taxation.

Revolting as they did against taxation and for liberty, is it to be wondered that many a man conceived of freedom as freedom from taxation and was prepared to carry on the fight against it even in a popular system of government? Resistance to taxation is a part of our political inheritance as well as of our economic, social, and folk inheritance. Smuggling, tax dodging, and rioting were instruments of defense, thoroughly approved of, and carrying no stigma of reproach. Some of the Revolutionary patriots were smugglers and tax dodgers. These facts reinforce the traditional attitude of resistance. They derive from a time when the American frontier was the Atlantic seaboard; they are attitudes of the frontiersman. But the frontier remained a definite location in some portion of America until the twentieth century, with the frontiersman active in the counsels of state and nation. Frontier conditions, frontier types, frontier attitudes toward government remain active to this day.

PIONEER SPIRIT STRONG IN NORTH CAROLINA

In considering North Carolina, therefore, we would do well to remember that this commonwealth started with a double measure of the pioneer, frontier spirit. Because of its lack of good harbors it was not settled as early as the northern colonies, nor, like them, directly from the old country. It was settled for the most part by way of the other colonies, at first chiefly from Virginia. People who in these older colonies had failed to find the opportunities they wanted, people who were not only dissatisfied with conditions in the old world but also with conditions as they found them in the older parts of the new world, came to North Carolina for a larger measure of individual, economic, and governmental freedom. North Carolina was the first pioneer state carved out of the wilderness by men who had already become Americans. Absorbed though it was in the British system, its beginnings were more like those of Tennessee and Kentucky than of Virginia. Its first settlers had an individualistic program of their own. They wanted a government suited to their means and ideas. They wanted cheaper and better lands, "elbow room," freedom to work out their destiny as a pioneer society. It was with these ideas in mind that they settled Albemarle in 1662.

But their land had already been set up by the king as a proprietary colony, and the proprietors interfered at once in their scheme of things. Instead of cheaper land, their rents were made higher than in Virginia. Regulations restricted their tobacco business more than in Virginia. They were not Anglicans but the Church taxed them. They saw their money going for government that gave them little in return by way of protection, stability, schools, roads, or any other institution of public welfare. Consequently they looked on the tax collector as a brigand and fought both openly and covertly against taxation. It is not surprising, therefore, that the whole history of North Carolina during the colonial period can be written around the struggle over rights and privileges, ways and means of taxation. The War of the Regulation was a struggle over taxation. The whole inception of the Revolution kept the question of taxation in the foreground of the public mind.

As North Carolina began to control its resources as an independent state, foresighted men began to plan institutions of education and welfare based on public support. From the beginning of our history there had been men of this type and they were to increase and prevail in the policies of the state. But parallel with this progressive and enlightened citizenship there remained the individualistic pioneer type—citizens who based their thinking on these age-old wrongs and emotions and doubted that taxation could ever be anything but injustice, and who continued to confront taxes imposed by their government with suspicion and evasion. Even so late as 1917 Governor Bickett could refer to our tax books as "a tissue of lies." And while he aroused the public conscience for a time, his work was short-lived.

Against this sentiment of resentment of taxation progress in our government has been slow. It has been difficult to get the citizen to tax himself, or even to realize that in a democratic government he does really tax himself. He has felt all along that some one else was taxing him and not for his good. Taxation

arouses class consciousness. The farmer, the laboring man, the manufacturer, the professional man—each thinks that his class is the victim of discrimination. He may be right about contemporary taxes, but his emotions at any rate refer back to some wrong in the experience of his class with taxation.

And thus, while we need to overcome our personal biases and our age-old prejudices in order to consider the tax question impartially and scientifically, while we must ascertain our objective as a self-governing people and measure our resources for investment in these objectives, we must prepare our minds for accurate estimates of these problems. But in order to go at the question scientifically, in order to arrive at expert knowledge, we must meet squarely and considerately these age-old obstacles to straight thinking about taxation.

THE RURAL TAX PROBLEM

CLARENCE HEER, *University of North Carolina*

Rural local government as embodied in our counties, townships, and school districts serves the needs of the country's most depressed and poverty-ridden economic group—the nation's farmers. With the average farm operator receiving less than $650 per annum for his labor and for that of his family, rural government ought to supply a maximum of needed services at a minimum of price. Actually, as at present organized and financed, it is the most expensive kind of government in the country.

That the American farmer pays out a larger percentage of his meagre income for governmental services than does the more affluent urbanite is abundantly evidenced by the findings of official surveys and reports. A report on rural taxation in Pennsylvania contains the following significant conclusion:

> Agriculture as a whole in the state carries a tax burden that consumes at least a 13 per cent larger share of the total earnings of the farm and the farmer than do all taxes paid out of the average earnings of the state with agriculture included in the average.[1]

A study made by a New York state legislative committee on taxation reveals the fact that local taxes absorbed 8.4 per cent of the net income of rural residents of that state in 1924, whereas they took only 4.7 per cent of the income of urban residents.[2]

The Federal department of agriculture has coöperated with various state agencies in measuring the burdensomeness of taxation on rented farms in different parts of the country. Its investigations show that the percentage of net farm rentals absorbed by taxes is alarmingly high in every state in which information was gathered.[3] In Michigan, on 1,018 farms, taxes took 55 per cent of the net property income in 1926. On farms in three counties of North Dakota taxes were found to take about 40 per cent of the net rent over a period from 1919 to 1924. In other states the percentages were as follows: Colorado, 33 per cent (1926); South Dakota, 30 per cent (1926); Virginia, 20 per cent (1926); Arkansas, 18 per cent (1921-1925); Indiana, 40 per cent (1923); Missouri, 20 per cent (1923); Ohio, 36 per cent (1919-1922). According to a recent study of the North Carolina Tax Commission, taxes absorbed 28.9 per cent of the net income of rented farm lands in this state in 1927.

Although the farmer spends a greater proportion of his income for taxes than does the dweller in cities, his return in governmental services is pitifully small compared with the corresponding returns of the urbanite. It is scarcely necessary to elaborate this point. Attention need only be called to such municipal services as police and fire protection, paved streets, water supply, sewerage, and garbage collection systems, most of which services the farmer cannot hope to purchase with his puny tax dollar.

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[1] "Some Phases of Taxation in Pennsylvania," *Bulletin Pennsylvania Department of Agriculture*, Vol. 9, No. 24.

[2] "State Expenditures, Tax Burden, and Wealth," *New York State Legislative Document* (1926), No. 68, p. 118.

[3] *Bulletin 346, Colorado Agricultural College*, September, 1928.

Practically the only substantial equivalent which the farmer receives for his taxes are the services of schools and highways. In North Carolina over 80 per cent of all rural tax monies are expended for those two objects. Since the farmer spends such a large proportion of his income for highways and education, it might well be expected that the quality of the rural offering in those two fields, at least, would be on a parity with current urban standards. That this is very far from being the case is almost too obvious to require demonstration.

In North Carolina, in 1926, over 11 per cent of all rural white children were still receiving their education in the antiquated one-teacher school. More than 19 per cent of them were receiving their schooling in two-teacher schools. Rural school property represented an average investment of only $95 per child, whereas in urban districts the investment in school property was $250 per child. The superior quality of instruction offered in the city schools was indicated by the fact that the average salary of urban teachers was $1,223 per annum, whereas rural teachers received on an average only $730 per annum. The average training of teachers in city schools was equivalent to three years of college work. The average training of rural teachers represented little over a year of college work. Rural high schools did not measure up to urban standards, as was evidenced by the fact that only 53 per cent of them were on the state list of accredited institutions, whereas over 95 per cent of all urban high schools belonged to that class.

Why does rural local government exact such heavy toll from the farmer and why does it give him such a small return for his money? Waste, extravagance, and inefficiency are undoubtedly important contributing factors. Governmental waste and extravagance, however, are not confined exclusively to our rural regions. City governments, too, may be sadly lacking in efficiency. To account for the wide differences in burdensomeness and operating results as between rural and urban governments, a more basic explanation is needed. This explanation is to be found in the nature of the functions which rural local government performs, in the size of the administrative units which have been selected to carry out those functions, and in the character of the revenue sources by means of which the functions are financed.

Basically there are two main reasons why the farmer is at such a serious disadvantage as compared with the city dweller in the matter of governmental benefits and burdens. The first of these reasons is connected with the fact that local governments in America are forced to rely almost exclusively on a single revenue source, the general property tax, as a means of financing their functions. Rural regions normally possess much less taxable wealth per capita than do urban areas. Therefore, in order to finance a given standard of expenditure per inhabitant, rural governments must apply a higher rate of property taxation and take a larger share of the taxpayer's income than the same standard of expenditure would entail in the city.

In the second place, the per capita cost of supplying what from the financial point of view are the more important governmental services is, as a general rule, considerably higher in the country than it is in the city. The unfortunate farmer is thus caught between the two sharp blades of a pair

of scissors. On the one hand, his tax rate is pushed up because he lives in a region in which wealth is spread out thinly. On the other hand, it is increased because rural populations are widely scattered and the resulting difficulties of organization make the per capita cost of government high.

LESS TAXABLE WEALTH IN RURAL AREAS

Of the two factors contributing to the extreme burdensomeness of rural local government, the low average of rural taxable wealth is probably the most important. In North Carolina, for instance, the twenty-five largest cities and towns had an average assessed valuation of $1,638 per inhabitant in 1926. For all the rest of the state, comprising mainly the rural regions, the average taxable wealth was only $834 per capita. In fact, in several rural counties the average taxable wealth was less than $500 per inhabitant. It will thus be seen that to raise a given amount of revenue per inhabitant in the rural sections of the state requires a rate of property taxation twice as high as is necessary to raise the same amount of revenue in the cities.

The fact that there is less assessed wealth per capita in the country than there is in the cities cannot be ascribed to the fact that rural property is assessed at a low percentage of its true value. The recent findings of the North Carolina State Tax Commission indicate that no class of property is, on the average, assessed at a higher percentage of true value than farm real estate. Nor is the differential between urban and rural values a phenomenon peculiar to North Carolina. In New York, in 1924, the equalized assessment value of taxable property amounted to only $1,156 per capita in the rural sections of that state, whereas it amounted to $2,001 per inhabitant in the cities.

The reason for the low per capita average of rural wealth is not far to seek. The bulk of this wealth consists of farm real estate, livestock, agricultural machinery, and household effects. The proportion of industrial, mercantile, and banking wealth listed on rural tax rolls is generally relatively small. Moreover, with the possible exception of industrial property, non-agricultural wealth in many rural regions is on the decline, owing to present day facilities for cheap and rapid travel which induce the farmer to transact more and more of his business in the nearest city. It sometimes happens that a rural county or township is peculiarly fortunate in having a large mileage of railroad trackage within its boundaries. In such cases, the burden on farm property may be considerably reduced. Instances of this kind are exceptional, however. As a general rule, agricultural wealth carries the lion's share of rural local taxation.

With the growth of industry and commerce, farm property is rapidly losing the importance it once possessed in the aggregate of the country's wealth. This tendency is strikingly illustrated in North Carolina. In 1910 farm property constituted about one-third of the total wealth of the state. By 1925 the proportion had dropped to one-fifth. At the present time the investment in manufacturing in the state is approximately equal to the investment in farms.

Nearly four-fifths of the tangible wealth of the state consists of non-agricultural wealth, comprising factories, warehouses, office buildings, banks,

mercantile establishments, corporate property of all kinds, and private residences. The cities, like huge magnets, exercise a powerful attraction on this form of wealth, drawing the bulk of it within their taxing jurisdictions.

Many of the business activities centering in the city are not in any real sense local enterprises. Their operations may be state-wide and even nation-wide in scope. Factories may sell their products in every state of the union. Mercantile establishments may draw their patronage from a broad area of surrounding rural territory. Jobbing and distributing houses may do no local business at all. Nevertheless, the fact that the property of such enterprises is physically or by legal fiction located within the confines of the city gives the city an exclusive monopoly over that property for purposes of local taxation. To the extent that taxes on business property are shifted to the ultimate consumer, city residents are placed in the enviable position of being able to enjoy governmental services which are paid for, partially at least, by outsiders.

GOVERNMENTAL SERVICES COST MORE

Even were there no complicating factors, the low per capita average of agricultural wealth would be sufficient to make the support of most rural governments an exceedingly burdensome proposition. As previously indicated, however, the farmer is the victim of an additional circumstance which still further increases the size of his tax bill. To supply the more important services of local government on a basis comparable in quality and quantity with prevailing city standards, normally entails a higher per capita cost in rural than in urban districts.

The foregoing statement may seem to be contradicted by the well-known fact that per capita governmental expenditures for urban areas are invariably greater, in the aggregate, than the corresponding figures for rural districts. Per capita total expenditures, however, furnish no indication of the relative costs of supplying identical services. The per capita expenditures of cities are high because the services they supply are greater in variety as well as superior in quality to the services available to rural residents. If consideration be limited to comparable functions, it is easy to demonstrate that per capita costs are as a general rule markedly higher in agricultural regions.

The reason for the higher per capita cost of rural local government admits of no easy and simple explanation. The fact that rural populations are thinly and irregularly scattered over wide areas is undoubtedly an important consideration, especially as regards the carrying on of functions whose cost depends on the extent of the territory to be covered. Thus regions where habitations are few and far between obviously require more miles of highway per inhabitant than thickly settled regions. The dispersion of rural population also affects the cost of public instruction. Agricultural communities are faced with the choice of maintaining numerous small schools easily accessible to the school population, or of transporting pupils over long distances to central consolidated schools. Both alternatives are expensive. The small school has an excessive overhead expense and provides an inferior kind of education. The consolidated school, covering a large territory, involves heavy charges for transportation.

The high per capita cost of rural government cannot be accounted for, however, solely on the basis of low population density. A more important factor is the matter of organization. Rural government is administered and operated by a multiplicity of agencies, each of which serves a comparatively small population group. North Carolina probably supports fewer local governmental agencies than many other states, since in this state the township and school district are of small importance and the chief functions of rural government are carried on by the county. Nevertheless, to serve the needs of a rural population which scarcely exceeds two million persons, North Carolina has set up no less than 100 separate county governments. Three of these counties had less than 5,000 inhabitants at the time of the last Federal census. Twelve counties had less than 10,000 inhabitants. Twenty-seven counties had less than 15,000 inhabitants and only thirty-four counties, comprising principally those containing cities, had populations in excess of 30,000.

A careful enumeration of the various conditions and circumstances which have resulted in organizing rural government on a basis of small population units is not necessary to the present discussion. Sparsity of population, topographical conditions, difficulties of transportation and communication, and local pride and particularism—all have doubtless played their part. Whatever the original causes, the important fact is that the typical agency of rural government is an exceedingly small-scale enterprise.

Small-Scale Operations

Small-scale operations in government, as in business, are usually attended by high costs per unit of product. There is abundant statistical evidence to warrant the generalization that most governmental functions are, up to certain limits, subject to the law of decreasing costs. Within those limits, the larger the population served, the greater the likelihood that personnel and facilities will be utilized to their maximum capacity, the lower the relative proportion of overhead costs, and the more numerous the opportunities for adopting the economical methods and facilities associated with large-scale operations.

The close relationship existing between the small population unit and high per capita costs may be illustrated by a few examples applying to widely different governmental functions. In the field of general administration the following conclusion of an Ohio research body possesses a high degree of significance.

> Of all the county agencies, the work of the general executive offices (auditor, treasurer, prosecuting attorney, recorder and county commissioners) is most standardizd in nature and extent. Yet the per capita cost of operating these offices is 50 per cent greater in the smallest counties than in the large ones. The average-size rural county pays about 30 per cent more per capita for performing these standardized services than do counties of more than 50,000 population.[4]

In the field of public poor relief the greater costliness of the small county, while not as strikingly evident, is nevertheless clearly apparent. Ninety counties of North Carolina maintain county homes or poor farms for the

[4] *The Ohio Citizen*, September 18, 1925, published by the Ohio Institute, Columbus, O.

aged, infirm, and indigent. Figures on the cost of operating these institutions are available for the year 1921. In counties having a population in excess of 50,000, the annual contribution per inhabitant required to maintain such homes amounted to 13.9 cents. In counties with populations between 30,000 and 50,000 the per capita contribution required was 14.6 cents. Finally, in counties with populations below 30,000, the average maintenance costs represented a burden of 15.1 cents per inhabitant.[5] Had it been possible to make proper allowance for differences in the character of the maintenance offered inmates at various institutions, the differential in favor of the larger counties would be much greater than appears from the figures. In some of the smaller counties, the county home consists of nothing more than a cheap cottage or shack with no conveniences or sanitary improvements.

A final illustration of the costliness of governmental agencies serving small population groups may be drawn from the field of education. Despite the fact that city high schools pay better salaries to their teachers and offer on the whole a better quality of instruction, it costs somewhat less (per child in attendance) to educate pupils in the city high schools of North Carolina than it does to educate them in the rural high schools of the state. The reason for the higher per-pupil costs in the country high schools seems to be due entirely to the comparative smallness of the average rural school, which in many cases renders it impossible to utilize the services of teachers in the most economical manner. In 1925, the average rural high school in North Carolina employed one teacher to every 17.4 pupils in daily attendance. The average urban high school, which was nearly three times larger, was able to get along with one teacher to every 20.3 pupils.[6] Had the rural schools been able to secure the same numerical ratio between teachers and students as the one in effect in the cities, they would have been able to cut down their per-pupil cost of instruction by 14 per cent.

The gist of the rural tax problem may be expressed in two sentences. Because rural communities are poor, the raising of a given sum of revenue requires a relatively high rate of taxation. Because rural governments serve comparatively small populations scattered over wide areas, a relatively large sum must be expended to produce a given result. These two tendencies explain why farmers in all sections of the country are complaining bitterly over the weight of their taxes, while at the same time educators and social workers are pointing to the low standards of rural governmental performance as a subject for state-wide concern.

Larger Administrative Units Needed

Is there any way out for the farmer? One obvious avenue of relief is to reduce the present high cost of rural government by increasing the size of administrative and operating units. The consolidation of small schools and the abolition of school districts as independent financial units have been going on apace. The extension of the consolidation idea to other fields of local

[5] *Special Bulletin No. 4*, North Carolina State Board of Charities and Public Welfare.

[6] See *Biennial Report* of the Superintendent of Public Instruction of North Carolina for the Scholastic Years 1924-1925 and 1925-1926, part IV, p. 21.

government is at least being discussed by legislators, though as yet it is rarely embodied in laws. A report on county government in Virginia, prepared by the New York Bureau of Municipal Research for the governor's committee on consolidation and simplification, recommends the immediate creation of administrative areas, consisting of two or more adjacent counties, in which certain county functions, such as schools, roads, health, and public welfare, will be merged under one administrative head. Complete merging of county governments is recommended in the case of unusually small counties.

A recent report of a special tax commission appointed by the legislature of North Carolina contains the following trenchant observations:

> The county as a unit basis for maintaining public roads is in the very nature of the case an uneconomic unit. Efficient and economic maintenance of public roads has become largely a matter of skillful use of expensive power-operated machinery, with a continually developing knowledge of technique in operation. County areas are not large enough to employ the use of such machinery at maximum efficiency. Knowledge of the most suitable machinery and the technique of operation cannot be developed by one hundred county boards, frequently changing, with the degree of efficiency of a central agency.

It will be expecting too much of consolidation, however, to rely on it to solve the farmer's tax problem. If recent experience in the field of education is to be taken as any criterion, consolidation may be expected to yield its dividends in the form of higher standards of governmental performance rather than in reduced tax bills. Consolidation will bring in more value for each tax dollar spent but, in view of the many inadequacies and lacks of present-day rural government, it is scarcely likely that any fewer number of dollars will be required.

As long as rural governments continue to have their present functions and as long as these functions are financed by means of a general levy on local property, the tax lot of the farmer will continue to be hard. Twenty-six per cent of the population of the country lives on farms. Agricultural wealth, however, represents only about 17 per cent of the country's aggregate wealth. The bulk of the tangible wealth of the country is invested in the instruments of industry and commerce, and under our present system of taxation this latter class of property is practically monopolized by the urban centers. Debarred from tapping the rich sources of industrial and commercial wealth, the position of the agricultural classes is comparable to the situation in which city wage workers would find themselves, if they were segregated into special districts and were obliged to finance the education of their children and other needed services through taxes on their cottages, flivvers, and radio sets.

LOCAL GOVERNMENTS AS AGENTS OF THE STATE

Friends of the farmer, people interested in equalizing educational opportunities and in raising rural standards in health and public welfare, are beginning to call attention to certain fundamental facts concerning the nature of local government and of the functions which it performs, the neglect of which facts, it is claimed, is in large part responsible for the existence of a rural tax problem. It is being pointed out that many of the most burdensome

of local governmental functions, such as education, highway maintenance, health, and public welfare, are, from an historical and legal point of view, not local functions at all but duties that devolve primarily upon the state. The adequate performance of these functions is a matter of more than mere local concern. It is affected with an interest which extends to the whole state. Even were this point of view not supported by history and law, it is claimed that the trend of modern economic development would nevertheless compel its acceptance. The integrating forces of the modern industrial era bind together the most widely separated communities by a multitude of economic ties. It is no longer possible for a locality to exist in isolated independence.

In carrying on activities which affect the interest of the people as a whole, local governments are merely acting as agents of the state. Their functions have been prescribed for them by the state, and their only financial resources for discharging those functions are such as the state allows them. The quality and effectiveness of their work are therefore dependent both upon the inherent difficulties of the tasks assigned to them and upon the adequacy of the financial resources which they are permitted to tap.

In delegating some of its functions to local governments, the state does not thereby relieve itself of the primary responsibility. It is still the duty of the state, as guardian of the people as a whole, to see that the powers it delegates are exercised uniformly and efficiently throughout its jurisdiction. This duty, moreover, imposes certain corollary obligations. The first of these is that the boundaries of local administrative areas be determined with some regard to the operating exigencies of the tasks to be performed. Administrative areas should be sufficiently large to permit the economic employment of modern facilities and technical methods. A second requirement is that local governments be held to some minimum standard of performance in the discharge of the duties assigned to them. Finally, since the state gives its local agents certain tasks to perform in accordance with certain minimum standards, it is on its part bound to furnish the financial support necessary to produce the required results. If this support is supplied through a delegation to the localities of a part of the state's taxing power, the resulting burdens should be uniform throughout the state. There would seem to be no valid reason why one class of citizens should be more onerously taxed than another class for the support of standard governmental services that are supplied in the interests of the state as a whole.

It is the failure to observe the last of these requirements which is chiefly responsible for the present tax woes of the farmer. For the purpose of financing services, the per capita costs of which vary considerably from place to place, local governments in America are in the main restricted to a single source of revenue. They are permitted to tax such property as happens to be located within their jurisdictions. Under such an arrangement it is impossible to secure any state-wide uniformity either as to services or tax burdens, except on one condition. The per capita taxable wealth in each local jurisdiction must be in proportion to the per capita amounts needed to supply that jurisdiction with the desired services.

When our present system of local government took form the condition stated was probably approximated. We were an agricultural nation and the territorial distribution of agricultural wealth is, as a rule, fairly even. Moreover, the services supplied by local governments were of a relatively simple and inexpensive nature. When public instruction was typified by the one-room school and when citizens contributed their personal labor toward the maintenance of the highways, there was slight room for local variations in per capita governmental costs. Nor, in view of the greater degree of local isolation, was there the same need as at present for uniformity in standards of performance.

The process of industrialization and urbanization has brought about a profound change in the factors conditioning local government. The territorial distribution of wealth is no longer even. Commerce and industry tend to concentrate in the urban centers. There are broad variations in average wealth as between one locality and another. The services expected of local governments are no longer of a simple and inexpensive character. The furnishing of many of these services now requires a highly trained personnel and expensive facilities. Where physical conditions or the smallness of administrative areas militate against the economic employment of such facilities, wide discrepancies in the quality of the services rendered or in the per capita cost of supplying these services are likely to appear. Finally, as all parts of the state become more and more tightly knit into a closely woven economic whole, the need for certain minimum standards in governmental services assumes increasing importance.

It is perfectly obvious that the maintenance of state-wide standards in the matter of services and of equality in the matter of tax burdens is not possible on the basis of the present method of financing local government. The ultimate solution of the rural tax problem depends upon the degree of success obtained in equalizing the burden of taxation as regards those standard minimums of various governmental services which are considered essential to the welfare of the state as a whole. Generally speaking, this equalization may be secured in two ways. The state may directly assume the functions it has hitherto delegated to the localities to perform or, without fundamentally disturbing the present system, it may equalize local tax burdens through the apportionment of grants-in-aid raised on a state-wide basis of taxation. Trends in state legislation show drifts in both directions. It may not be unreasonable to hope, therefore, that the farmer may eventually be extricated from his present tax difficulties as a result of further progress along the lines indicated.

THE PROPERTY TAX PROBLEM

RALPH C. HON, *Missouri*

The problem of taxation is always of general interest, but it is particularly so in North Carolina at the present time because of the fact that the widespread recognition of the need for reform led Governor McLean, on July 5, 1927, to appoint a special tax commission to gather information on the entire state tax structure, such information to be submitted to him for transmittal to the 1929 general assembly.

In his 1927 message to the assembly the Governor made this statement, "The most serious phase of our tax problem arises in connection with local taxation. Every thinking man and woman knows that personal property and real estate, whether devoted to home, agricultural or manufacturing uses, is bearing too heavy a burden of taxation in many of our counties. In some counties taxes on farm lands are out of proportion to the earning capacity of these lands.... For a community to discourage and hamper agriculture or to drive manufacturing plants from its borders through burdensome taxation is nothing less than stupid." Commissioner Maxwell, in an address before the North Carolina Club, November 1927, is quoted as saying, "No state in this country has gotten very far from the property tax as the chief dependence for revenue. It is much the most important form of taxation in North Carolina and one that has not been given the importance and the attention that it deserves." It is with this tax that the present paper will be concerned. To be concrete, the importance of the general property tax in the State of North Carolina is indicated by the fact that ninety-seven per cent of the revenue of the counties and their subdivisions is derived from this source. It is peculiarly essential that the people of the state give this particular source of revenue careful consideration in the near future because it will be their duty, in November, to vote upon a proposed amendment to the state constitution which would permit the general assembly to classify intangible personal property and give it a lower rate than that on tangible property.

Professor Seligman has given considerable attention to the history of the general property tax in different countries and concludes that its use has been universal in agricultural communities but that its discard has been equally universal as a more complex economic structure has been attained. He found that in the year 1166 a property tax was levied throughout almost all Europe to aid the Crusaders. The system seems to have been moderately successful because the period was one in which there was slight differentiation of property. But as early as 1694, in England, Briscoe wrote that gentlemen (whose estates were in land) were pressed with taxes, while the monied men were in a manner tax-free. In the eighteenth century such criticism became commonplace. In 1833 the English tax on personal property was repealed.

It is interesting, in looking over the old laws of North Carolina, to find that the second act passed by the assembly (which met in New Bern, April 8-9, 1777) after the Declaration of Independence, was entitled "An Act for levying a Tax by General Assessment" and contained this statement: "Be it Enacted—

That a Tax of one half of a Penny be levied on each Pound Value of all the Lands, Lots, Houses, Slaves, Money, Money at Interest, Stock in Trade, Horses and Cattle, in this State." Rather elaborate machinery was provided to assure collection.

Due, in all probability, to the power of the wealthy class, a small poll tax was soon substituted for the property tax on slaves and gradually other forms of property became exempt, until practically all revenue was derived from a tax on land and polls.

APPEARANCE OF GENERAL PROPERTY TAX

The truth seems to be that taxes, a century ago, were so insignificant that little attention was given to the basis on which they were levied. In Governor Swain's message of 1833 we find him reproving the legislature for not spending more money, "That government cannot be wisely administered where those who direct the expenditure of the public treasure receive more for this service than the amount of their disbursements. I urge the propriety of entering upon a system of legislation required by the wants of your constituents, commensurate with their resources, and worthy of the confidence which they repose in your ability to administer their public affairs." In 1835 the same governor said, "The history of state legislation during the first half-century of our political existence, will exhibit little more to posterity than the annual imposition of taxes amounting to less than a hundred thousand dollars, one half of which constituted the reward of the legislative bodies by which they were levied, while the remainder was applied to sustain the train of officers who superintended the machinery of government. The establishment of schools for the convenient instruction of youth, and the development and improvement of our internal resources by means beyond the reach of individual enterprise, will seem scarcely to have been regarded as proper objects of legislative concern." It is a matter of record that the state rate of six cents on the one hundred dollars worth of lands and twenty cents on the poll remained unaltered for over thirty years, and was not increased until the year 1854. However, local taxes rose rapidly after 1847 and the people soon demanded that other property, including slaves, be taxed at property rates. Their attitude is well stated by one of their state senators (General Edney), "The just and equitable principle of ad valorem taxation, is the only one that will do equal justice to all men, the high and the low, the rich and the poor, the noble and the ignoble. This system taxes every species of property that mortal man owns, according to its true value, and of this no man can complain." The main issue centered exclusively around the question of taxing slaves, but general ad valorem arguments were presented. The result was that the constitution of 1868 contains Article 5, Section 3, which is to the effect that "All property shall be taxed by a uniform rule at its true value in money," even though there were no longer any slaves to be taxed.

At that time the constitutions of practically all of the states contained a clause of this nature, which is generally known as the uniform rule, but one by one they have abandoned it until now only sixteen are thus restricted. Of these, Illinois recently took a vote on the question and a majority voting on

the amendment favored the reform, but not a majority of the total number of voters, as is required in that state. Ohio has also tried to free herself of the restrictions but has thus far been unsuccessful. In 1914 a determined effort was made in North Carolina to secure a constitutional amendment authorizing general classification of property for taxation. It seems to have had the support of practically the entire press of the state and was publicly supported by many of the leaders of thought. But it was opposed by the chairman of the State Corporation Commission, who issued a general statement about three weeks before election day attacking the amendment in a vigorous manner. The vote was 50,520 to 68,148. Ten separate propositions to amend the constitution were up at the same time and each and every one was defeated. This may have been due to extreme conservatism in regard to changing the basic law of the state, but the more plausible explanation seems to be that thousands who had no opportunity to become acquainted with so many propositions, many of them complicated and confused by claims of contending factions, decided to play safe and vote "no" on everything. Thus there appears to be some ground for the belief that the failure of the proposed amendment was due to the confused manner in which it was presented.

WIDELY CONDEMNED NOW

The general property tax has been the object of severe, unrestrained, and almost universal criticism. One could easily fill a book with such statements as the following, which is taken from a report of the Louisiana Tax Commission: "The system is condemned by political economists writing from a theoretical standpoint; by practical tax officials, speaking from actual experience; by dozens of tax commissions appointed to investigate its workings. Indeed, its failure is shown by testimony overwhelming in quantity, unimpeachable in quality, and so far as we have read, without a dissenting voice."

One does not have to seek far for an explanation of this breakdown, as many valid reasons have been presented.

1. All of the outbursts of oratory which proclaimed the fairness of the general property tax three-quarters of a century ago were based on the assumption that all types of property confer upon their owners the same amount of tax-paying ability. While this may have been relatively true when property owned by various individuals was comparatively homogeneous, both in quantity and quality, it certainly is not true in 1928 in North Carolina with its innumerable varieties of property with their vastly different yields. According to a report of the state board of agriculture, something over two-thirds of the territory of the state was classified as forest land in 1920. Vast quantities of this land will provide no income for many years and but little then. Competent observers state that much of this land would not sell for enough to pay the back taxes levied against it. (This problem is especially acute in the eastern part of the state, where the boll weevil has ruined the chief staple, the land is not suited to tobacco, and the lack of nearby markets threatens the chief truck crops.) Two farms or two cotton mills, each of the same value, may meet with vastly different fortunes during the year, not to mention forest lands as compared to successful commercial enterprises.

2. Even if all property were endowed with equal tax-paying ability, there would still be the troublesome question of incidence. The theory has become well established that some taxes can be shifted consistently. Among the factors which have weight in deciding who bears the burden are elasticity of the demand for the commodity, mobility of the capital concerned, durability of the object, extent of territory over which the tax is operative, extent of competition, and rate of the tax. It is easily seen that if the question of who pays the tax depends upon these—and various other—influences, the idea of justice in a general property tax goes by the board.

3. The system assumes not only that all property is equally productive but that the different varieties may be assessed with equal facility. This position is obviously untenable. It is comparatively easy, with the aid of tax maps, to locate all real property, but attempts to find such intangible items as bonds, mortgages, and even bank deposits, have met with little success. In case the state should adopt a vigorous policy of law enforcement the result would be merely to drive much-needed capital beyond the limits of her borders.

4. Since farmers have occupied a relatively poor economic position during recent years and their property consists more largely of tangible property than does that of any other group, and since the general property tax is most effective against such property, it follows that the tax is regressive. This reminds us of an eighteenth century statement of Walpole's: "It is safer to tax real than personal property because landed gentlemen are like the flocks upon the plains which suffer themselves to be shorn without resistance; whereas the trading part of the nation resembles the boar, who will not suffer a bristle to be pluckt from his back without making the whole parish to echo with his complaints."

5. Of all the criticisms against the tax under discussion, probably the most pertinent, from an ethical viewpoint, is that it constitutes, by its very nature, an incentive to dishonesty. The average rate in the state is slightly over two per cent, which constitutes a burden on four per cent investments (for example, bank deposits) equal to that of a fifty per cent income tax. Most property owners appreciate the value of the services rendered by their local governments and are willing to assume their fair share of the burden, but when they realize that other people are not listing property which can be hidden they find it very easy to justify themselves in following a similar policy as a matter of self-defense. Thus we account for the fact that men of considerable social conscience, "men who would die for their country, will lie for their taxes." In this manner perhaps a majority of our taxpayers render themselves guilty of perjury, since each person who lists property must sign the following oath, "I do solemnly swear that the above and foregoing listed property is a full, true and complete list of all and each kind of property owned by me or under my control as agent, guardian, personal representative or otherwise—so help me God." This is responsible for the remark frequently heard that "If it is true that Jove smiles at the vows of a lover, it must be true that he laughs out loud at the oath of a taxpayer." North Carolina state officials have long recognized the seriousness of this situation, which has changed little in the last century. The message of Governor Swain in 1834 contained this

passage, "The Government of the country should never hold out temptations to its citizens to do wrong. Such, however, is the manifest tendency of the most important principles of our fiscal system." And in Governor Bickett's frank and telling appeal for revaluation in 1919 one finds the following, "We may not hope to be a great people so long as we condone falsehood and deception in our relations to the Government under which we live. The principles and practices that are tolerated in the listing or non-listing of property for taxation constitute a school of immorality that will, if allowed to continue, destroy the moral fibre of our people." When one attempts the formulation of definite suggestions, the adoption of which could be reasonably expected to lead to general conditions of marked superiority over those existing at present, he is on less solid ground. Tax advisers try not to be so crude as to resort to the old rule for distinguishing a toadstool from a mushroom but, after all, most of our knowledge of taxation has been gained through trial and error.

GRADUALLY SUBSTITUTING INCOME AS A BASE

One plan, of which more will probably be heard in the future, provides for an increasing use of income or yield, rather than property, as a basis of taxation. This is suggested with approval by Professor Seligman in his *Essays in Taxation,* recommended by the Manitoba Special Commission on the Real Property Tax (1925), and sponsored by Secretary Jardine in his annual reports to the President.

Farm taxes are levied almost entirely on the basis of capitalized value and bear little or no direct relation to current farm earnings. It is a matter of common knowledge that in the disastrous years since the war many farmers in all parts of the country have failed to make their taxes. It is estimated by the National Bureau of Economic Research that the income of farmers in the State of North Carolina in 1920 was four hundred and fifteen million dollars, while in 1921 it was only two hundred and thirty-five million. This represents a decrease of forty-four per cent in one year.

A few states are relieving the burden in farm property by returning a part of the income, inheritance, and other special taxes to the local districts in which they were collected. The State of New York, for example, returns fifty per cent of its income tax in this manner and Wisconsin follows a similar practice. North Carolina's educational equalizing fund serves somewhat the same purpose, although it is distributed on a different basis. It would seem that this fund might well be augmented, perhaps through the reduction of exemptions in calculating income taxes and applying the additional income to this purpose. This would not only afford some relief to owners of real property but would likely aid in enlisting the coöperation of the great lower income bracket group in exercising closer supervision over the expenditure of public funds, which, according to no less an authority than Professor Bullock, must receive increasing attention from all those interested in the fiscal affairs of our state and local governments.

A large part of the problem in North Carolina originates in the unequal distribution of wealth among the different counties. The spread is from

approximately $400 to $1,800 per capita. Both the revenue and the cost of rendering governmental services vary from county to county, but they do not move together. McDowell County obtains 39.2 per cent of its revenue from public service property, while Dare County has no such property. In so far as Dare people patronize McDowell railroads they help pay the taxes of the latter county. A few fortunate counties also receive large amounts of taxes from industrial corporations which do business all over the state. It appears that some relief might be afforded were the state to take over the taxation of these concerns and distribute the proceeds on a different basis.

CLASSIFICATION OF PROPERTY

About thirty states now have some form of classified property tax, but the classifications are so diverse that it is difficult to draw conclusions as to the effectiveness of each. By giving property that is less productive or more easily hidden the benefit of a low rate, many states get larger amounts of such property on the tax lists than was formerly thought possible. In a few instances this increase has been great enough to produce an enlarged revenue in spite of the low rate. A strong case can be formulated for treating intangibles in this manner. No government has ever been able to get such property on the tax books at high general property rates, and it would be an abuse if it were accomplished. Most intangible wealth merely represents specific tangible property which is taxed, and to that extent taxation of intangibles involves double taxation. But even in the case of intangible property which is not merely representative, such as money, the rates are often confiscatory. If intangibles pay at all, they are assessed at their full value in most cases. For example, a note has its value clearly indicated on its face. This encourages evasion because the holder realizes that real estate is being assessed at only a fraction of its value. This evasion, in turn, causes higher rates and pressure for still lower valuation of real estate. Thus the 1926 report of the Ohio Joint Legislative Committee on Economy and Taxation concludes that "by preventing the taxation of intangibles at rates sufficiently low to secure an adequate listing of them, the uniform rule makes impossible the checking of the ever increasing burden on real property. Under modern conditions the general property tax tends to become more and more a tax upon land and buildings and with the barrier of the uniform rule confronting it no legislature can do much to change the condition." It would obviously be presumptuous for the present writer to question the conclusions of the Ohio Committee for their own state, but he feels justified in expressing the opinion that if the Committee is correct in thinking they could secure greater revenue by granting a low rate on intangibles, the present administration in Ohio is not as efficient as that in North Carolina. This study reaches the conclusion that increased revenue under low rates has resulted only where the assessments were conspicuously low before classification.

Minnesota is the classic example to which proponents of classification always point with pride. It is true that from 1910, the year before she adopted classification, to 1926 her assessed intangibles increased from fourteen million to four hundred and fourteen million dollars and her revenue from in-

tangibles increased from three hundred and eighty thousand to one million two hundred and forty thousand. Equally significant is the fact that the average collection from citizens paying on intangibles dropped from $61.25 to $10.78. This indicates that from the standpoint of justice to the honest taxpayer Minnesota has a very superior system, but in spite of the fact that the accompanying statistics indicate that there are more than twice as many intangibles in the state of Minnesota as there are in North Carolina, the latter state collects double the amount of revenue secured by Minnesota from that source. Thus it seems clear that Minnesota's remarkable improvement is explained, in a greater measure, by the fact that her previous system was strikingly inefficient rather than by the claim that the present order possesses singular merit.

From the standpoint of revenue, Kentucky seems to have the best record, in proportion to her wealth, that we were able to find among the states that have classification. (Statements in the 1925 report of their tax commission would lead the unwary reader to believe that the performance is even better than it is.) However, Kentucky adopted classification in 1917 and it was not until 1924 that intangibles bore as large a revenue as they had previous to classification. Even then the increase seems to have been due largely to the findings and recommendations of the 1923 Efficiency Commission.

The following figures appear to be significant:

	North Carolina	*Minnesota*	*Kentucky*
Bank deposits	$358,857,000	$905,728,000	$397,939,000
Dividends	26,782,547	47,296,063	31,503,510
Interest and inv. income	8,233,978	30,495,922	11,997,802
Assessment of intangibles	162,404,883	414,000,000	842,438,200
Revenue from intangibles	3,248,097	1,240,000	2,848,050

The bank deposit figures are taken from the *Federal Reserve Bulletin* and are for June 30, 1926. The dividend and interest figures are from the Federal Income Tax returns of 1925. The assessment of intangibles and revenue from intangibles figures for Minnesota and Kentucky were obtained from reports of their tax commissions. The "net solvent credits" item in the commissioner's report was taken as constituting the intangibles for North Carolina. The figure for revenue is an estimate secured by taking two per cent (slightly less than the average rate) of the net solvent credits. This estimate is probably a little high, since "net solvent credits," as interpreted by the tax authorities, includes some farmers' inventories; but it is thought that this item is not large enough to affect the conclusions that may be drawn from the table.

We conclude that the adoption of the proposed amendment would be almost sure to result in a moderate loss of revenue from intangibles, at least temporarily, but that if the state is willing to make that sacrifice in the interest of a more equitable system of taxation, the amendment might well be supported. We regret that the wording does not provide for a classification which would relieve forest lands.

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THE ASSESSMENT OF RURAL REAL ESTATE IN NORTH CAROLINA

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Introduction

From time immemorial governments have collected funds in some manner from their citizens to bear the expenses of common causes. One of the first things to be taxed was real estate. Professor Seligman, in his *Essays on Taxation,* says, "everywhere at first the direct property tax is found to be the land tax or the tax on agricultural capital."[1] Even today real estate is the backbone of our present system of taxation. Sixty-six per cent of all the taxes collected in the counties in North Carolina in 1926 was derived from real estate. The taxation of real estate has been uninterrupted. As time passed various suggestions have been made that this tax and that tax be abolished or substituted, but no one has ever suggested that we abolish the tax on real estate. Real estate is visible and makes a fine object for taxation. The fact that other things can be more easily hidden and can better elude the tax collector has led to real estate being the ultimate source of revenue for a long time.

Regardless of the fact that real estate taxation is an ancient practice and is the backbone of our taxation system, it is probably one of the most criticized forms of taxation. The practice of assessing and taxing real estate has been in use long enough to approach perfection now, but, nevertheless, it contains numerous weaknesses and is justly criticized. The chief complaints are the highness of taxes and the inequality in taxation. The first draws less criticism than the second. Of course, a great kick is raised against excessive taxation, but so long as the tax does not bring a very great financial burden to bear upon the citizen, he will not complain nearly as severely as he will if his property is being taxed at 30 per cent and his neighbor's property at only 20 per cent. As a matter of fact, high taxes are not infrequently caused by inequalities. The money has to be raised and if one farm is undertaxed, then another must be overtaxed. Under ordinary circumstances and during normal times a scientific assessment would eliminate both of these complaints.

The taxation of rural real estate may be said to be extremely backward throughout the United States. Only recently has any scientific method of assessment been successfully attempted in any of the states, and even yet none can be said to have advanced very far. The assessment of urban real estate has advanced more rapidly, and is at present fairly scientifically handled. Rural real estate methods have not kept the pace set by urban and yet they should be ahead of urban, for much more money is derived from the taxation of rural real estate than of urban. Figures in the report of the State Board of Assessment and the State Board of Revenue of North Carolina show that, in 1925, of the $1,795,327,538 assessed valuation of real estate only $732,657,042,

[1]Seligman, *Essays on Taxation,* p. 11.

or 41 per cent, was attributable to urban real estate. It is worthy of note that all towns—regardless of size—are included in the estimate of urban real estate. In view of the fact that rural real estate is of such great importance in North Carolina, it should be assessed in a more scientific manner. The assessment and taxation of real estate are as much of a science as the valuation of public utilities, and should be handled in a fair and accurate way. At present the system in North Carolina, as will be shown later, does not even approach being scientific. The system is unfair, inaccurate, and antiquated.

Assessment of Rural Real Estate in North Carolina

What is the system of assessment in North Carolina? According to law it is one thing and in practice it is another. The law as to assessment in North Carolina is somewhat as follows: the title of the state supervisory agency is the State Board of Assessment, which is composed of three members. This board has the power to review original assessments upon complaint of the taxpayers, but not upon their own motion.[2] This board is also without the power to order reassessments.[2] It is the duty of the Board to confer with assessing officers as to their duties and to supervise them in general. At least thirty days previous to the date for listing taxes the Board is required to prepare a pamphlet of instructions to tax assessors. The Board has the power to require from any officer in the state, on forms prescribed by it, such reports as will aid assessors in obtaining a fair assessment. Forms to be used in assessing and listing property are prepared by the State Board of Assessment and transmitted to the Commissioner of Labor and Printing. From here they are sent to the boards of county commissioners, and thence to the assessors and list-takers.

The supervisory officials of the county are the members of the board of county commissioners. This board appoints a resident free-holder as county supervisor. If a county has an all-time tax official, he becomes the supervisor. The supervisor appoints an assistant in each township.

The above is an outline of the structure of our system as to officers and their duties and powers. The working of this organization falls, more or less, into two parts: the annual list-taking and the quadrennial assessment.

Annual List-Taking

Each year the assistants to the county supervisor post notices requiring all taxpayers to list their property. It is the duty of the township list-taker and assessor to determine by visitation, investigation, or otherwise, the actual cash value of each piece of property in his township. The township assessor has the power to administer oaths. All property listed by taxpayers is listed under oath, and any taxpayer refusing to answer questions respecting his property or to swear to his returns is guilty of a misdemeanor. The list-takers and assessors also work under oath. They are required to take an oath to list and assess property at its "true value in money." This phrase, "true value in money," has been interpreted as meaning the value of property when sold,

[2] *Summary of Farm Real Estate Assessment Procedure in the United States*, Agricultural Experiment Station, Michigan State College, 1927.

not at a forced sale, but in such a manner as it is usually sold. After the assessment list is prepared and passed upon by the supervisor, it is turned over to the board of commissioners. This board is also the board of equalization and is supposed to make corrections where property has been incorrectly assessed. The record of the proceedings of the board is sent to the State Board of Assessment. An appeal can be made to the board of county commissioners by the taxpayers, and can be carried still farther to the State Board of Assessment.

After the list has been turned over to the board of county commissioners it has two copies of the tax list, as revised and settled, made out by the register of deeds, auditor, tax clerk, or other official performing this duty, according to blanks furnished by the State Board of Assessment. One of these copies remains in the office of the clerk of the board of county commissioners and the other is delivered to the sheriff or tax collector. The auditor, register of deeds, tax clerk, or other official performing such duties is required, after the list is deposited with him by the board of county commissioners, to return to the State Board of Assessment and the auditor an abstract of the same.

The Quadrennial Assessment

The second important part in the working of the taxation organization is the quadrennial assessment. Every fourth year property is reassessed to take care of any changes in value which have occurred since the last assessment. The supervisor, appointed by the board of county commissioners, has charge of the township assessors. He appoints three freeholders in each township as a board of assessors or a single assessor. This board or individual is to list and assess all property in the township at actual full value. These assessors and the supervisor meet in the county courthouse before assessing and decide upon methods whereby to obtain uniformity and accuracy in assessment. The board of county commissioners can, upon the request of the supervisor, hire experts to assist in the assessment. In determining the value of property the location, quality of soil, quantity of standing timber, water privileges, water power, mines, minerals, quarries, and other valuable deposits are considered along with the fertility and adaptability of the property to agricultural and commercial uses. The assessors are also to consider the income derived in the past and the probable future income, as well as the past assessment. The assessors convene after the assessment to make certain that uniformity exists. The prepared roll is given to the board of county commissioners, which serves as the equalization board. The channel of appeal by the taxpayer is also the same as in the case of personal property.

Assessment Practices

The above is a rough synopsis of the way in which list-taking and assessing would be done in North Carolina according to law. The general plan is very well followed in practice, but certain details of the law are not carried out. First of all, the section which requires that all real estate be assessed at full value is not enforced. The ratio of true to assessed value varies greatly in North Carolina upon different pieces of property. It was found by the

Revaluation Committee of 1919 that farms were assessed at $2,030,000,000 less than actual value.[3] It was also found that 5 per cent of the farms were over-assessed. This failure of the assessed value to correspond to the true value is found in practically every state having the system of taxation used in North Carolina. The fact that the assessment is not in accordance with the law is deplorable enough, but it is still worse when we consider the gross inequalities existing among the taxpayers. The fact that property is under-assessed would not be so bad if all property were under-assessed in the same ratio, but as it is we have one farm assessed at 20 per cent of its value and another at 80 per cent. It is such discrimination as this which brings the greatest criticism upon our system of taxation. Why do these inequalities prevail? Mainly because of the awkward manner in which property is assessed. As a rule, the assessor carries around a tax list, asks the taxpayer what his property is worth, has the taxpayer swear to its value, takes down the figures, and goes on to the next farm. It is very rare that the assessor is energetic enough to make a thorough investigation to determine the actual value. In the cases in which he does make a direct estimate it usually results in an unfair assessment for one man as compared to another, for the tendency is for the assessor's idea of value to change from day to day, and from farm to farm. It is very seldom that either the assessor or the owner knows the value of the farm. There is an absence of standards by which to judge. The whole thing is very nearly guess work. The assessor is generally ignorant of the value, and the owner, if he knows the value, hesitates to reveal it. In 1924 there were 1,400 people apprehended who failed to list property owned in Durham County alone.[4] One could hardly blame a taxpayer for inaccurately valuing his property when his neighbor and many others are being under-assessed. To value it correctly would be to subject himself to a part of the tax burden which others should bear. It can safely be said that almost all of the trouble arises from the lack of importance assigned to the office of assessor. He is unqualified, unequipped, and underpaid. Not underpaid for what he does, but the salary paid does not attract men of the calibre needed. Assessors are, as a rule, not of the more capable class of citizens in North Carolina. It is a position which few are anxious to have, and consequently it falls into inefficient hands. The supervisor himself is often not paid over $200.00 a month, and the salary paid his assistants is so meager that it is pathetic to see the class of men in whom the power of list-taking and assessing is vested. The assessors do a poor job and one could hardly blame them. A man usually assumes responsibility according to the amount he is paid and according to the impression he receives of the importance attached to the work he is doing. The assessors assume very little. They have very little equipment to work with, usually very little education, and few standards to go by in making their assessments. The absence of standards leads to the inequalities mentioned, which will be discussed later. The lack of standards causes assessors to be influenced by outside factors and to rely very heavily upon former

[3] *Report of Revaluation Committee*, 1919.
[4] *Durham Herald*, December 30, 1924.

assessment rolls in determining values. Raising revenue for a government is decidedly too important to be handled carelessly, and should be more scientifically conducted.

ASSESSMENT OF SMALL FARMS CONTRASTED WITH LARGE ONES

This system has long been criticized, and every year for the past few years the report of the State Board of Assessment carries recommendations for improvements. There is a strong appeal that we abolish the inequalities resulting from the present system.

One of the most outstanding evils is the discrimination made in the assessment of small farms as contrasted with that of large ones. The assessor, without any standards by which to judge, will invariably assess small amounts of property at a higher rate than large amounts. A study of several counties in Pennsylvania showed that in nearly every case the small farm was more highly assessed.[5] One of the most extreme variations was in Westmoreland County where property valued at $2,500 and less was assessed at 91 per cent of its value and property valued at over $100,000 was assessed at 27.4 per cent. This was an unusual case, to be sure, but taking into consideration the majority of the counties, the rate varied about 25 per cent in the assessment of large and small farms. "The ordinary assessor, working as he not infrequently does on part time, without previous training, without system and without adequate records, can guess at values more closely in the case of small properties such as those he lives near, and similar to those he may have himself owned, built or sold, than he can at the value of properties with which he has had no first hand experience."[6] An assessor can usually tell very accurately how much a few acres of land are worth, but his idea of the value of many acres is vague. The Efficiency Commission of Kentucky states that it is a universal tendency for small parcels to be more fully assessed than large ones.[7]

ASSESSMENT OF VALUABLE LANDS CONTRASTED WITH THOSE THAT ARE LESS VALUABLE

A second inequality, very similar to the one just discussed, is the one existing in the assessment of valuable lands as contrasted with the assessment of lands having little value. By this is meant that land which yields a large income is not taxed as high in proportion as land which yields a small income. Turning again to the Pennsylvania study of 1926, we find that taxes on business and residence property represented 17.5 per cent of the net income derived from that property, while taxes on owner-operated farms represented 33.9 per cent of the income derived.[8] The same is found to be true when the assessment of farm lands in North Carolina is considered.

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[5]Weaver, *Rural Taxation in Pennsylvania.*

[6]Buck, *Municipal Finance* (author is a member of National Institute of Public Administration and New York Bureau of Municipal Research).

[7]*Report of Efficiency Commission of Kentucky,* 1924, p. 232.

[8]Wheeler, *op. cit*

INEQUALITIES BETWEEN TOWNSHIPS

One of the most interesting observations in the field of assessments is the variation in the opinion of two assessors as to the value of the same piece of property. There is nothing unusual about this, yet when two assessors estimate the value of similar farms differently a gross inequality results. A very interesting example of this is shown by an incident which took place in New Jersey.[9] Two assessors became confused as to the line between their respective districts. As a result, both assessed separately a piece of property which each believed to be in his district. One turned it in at $350 and the other assessed it at $1,050. Examples of this kind are numerous, and there is no doubt but that an investigation would reveal similar conditions existing in North Carolina. A case in Kansas still further illustrates the point. In showing the values fixed upon adjoining tracts, separated only by the township lines, the following figures were obtained:[10]

Township line	137	149	129	116	96	70	91	82	70	76	73	71
	78	75	76	62	52	44	45	47	44	44	40	53

(Read across township line)

Such discriminations as these have existed much too long both in North Carolina and elsewhere. Some remedy should be produced.

INEQUALITIES IN THE SAME TOWNSHIP AND BETWEEN COUNTIES

Two other similar types of inequalities are those existing between one county and another, and between taxpayers in the same county. The former is not nearly so bad as the second, as long as the county is the unit of taxation. Nevertheless, it would be better if assessments in different counties could be similar. The inequality in the assessment of two farms within the same taxing unit is of course indefensible. This inequality is probably the subject for the greatest complaint.

During the revaluation of 1919 two farmers, each owning a farm in a certain mountain county and in the same neighborhood, were found to be taxed at $600 each. The committee discovered that one farm had 50 acres and the other 12 acres. When questioned, the farmer having the 50-acre farm swore it was worth $4,000 and the one with the 12-acre farm swore it was worth $650. Similar situations exist all over North Carolina today and should be corrected. Such variations in valuations are not because of different opinions, for the work is all done by one assessor. The fault lies in the fact that the assessor is not equipped for the work. He has no convenient means of knowing how many acres there are in a farm. He has no correct records to go by and has no standards by which to measure value. If the assessor were furnished a record of the number of acres in each farm, the kind of land of which the farm is composed, and a table of value by which to assess that type of land, he would come much nearer to obtaining uniformity in his valuations.

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[9] *Proceedings of National Tax Association*, VI, 33.
[10] Lutz, *State Tax Commissioner*, p. 435.

Needless to say, these inequalities produce a very unfair distribution of the tax burden. Some bear more than their just share of the tax burden, others do not bear their full portion, and some escape almost entirely. This system makes what could be a reasonable tax rate one which is met at a sacrifice by some because others are not bearing a fair portion. More uniformity is the goal to be attained.

UNDER-ASSESSMENT OF LAND

There are still other criticisms which can be made of the present system. First of all, much land is under-assessed. A large amount of revenue is thereby lost. This under-assessment exists in nearly all, if not all, of the state. Some land may be over-assessed, but more is under-assessed. In no case is it assessed at more than two-thirds of its value in Massachusetts, and in some cases the ratio of assessed to true value is only 30 per cent;[11] and yet the law requires assessment at full value. In Oregon the ratio of assessed to true value is 60 per cent.[12] Figures collected by the railroads in 1920 show the following facts concerning the ratio of assessed to true value in several counties:[13]

	Per Cent		*Per Cent*
Carteret	98.66	Cherokee	65.39
Henderson	87.12	Stokes	59.20
Clay	71.51	Surry	54.86
Forsyth	71.34	Davidson	54.02
Guilford	70	Washington	51.95
Buncombe	69	Bertie	50.46
Durham	68.40	Wayne	35.91

In these cases true value was based upon sale value. The extreme variation in the ratios occurs in the cases of Carteret and Wayne. Here we have a difference of 62.75 per cent. This is absurd when it is considered that both counties are in the same state and supposedly assessed under the same law. Another contrast almost as bad is an assessment in Forsyth at 71.34 per cent while the adjoining county, Stokes, was assessed at only 59.20 per cent. According to the railroad study mentioned above, the ratio of assessed to true value could not be much over 75 per cent throughout the entire state. Figures published by the Bureau of the Census placed the ratio at 75.7 per cent for the year 1922.[14] The loss of revenue by under-assessment is sufficient cause for severe criticism, but the fact that the ratio is not the same in any two counties is the cause for more alarm and should be convincing in showing that the present system is not functioning properly and therefore needs revision.

OMISSION OF LAND FROM TAX RECORDS

Of still more serious consequence is the fact that not only does some land partially escape taxation by under-assessment, but many acres are entirely

[11] *Bulletin of the National Tax Association*, January, 1927, p. 96.
[12] *Report of the Special Tax Investigation Committee*, 1925, p. 7.
[13] *Durham Morning Herald*, January 28, 1922.
[14] *Estimated National Wealth*, Bureau of Census, p. 5.

omitted. At first thought it is almost unbelievable that land in a state which has been making assessments for scores of years does not even appear upon the tax book. It is nevertheless true. The Revaluation Committee of 1919 had this to say after it had completed its work: "Quite the most surprising item in the list is the discovery of 1,032,290 acres of land which was contributing no part to the public expense. This, in itself, is sufficient condemnation of the former indifferent methods of listing property, and points to the necessity of finding some means by which a piece of real property once on the tax list can never get off."[15] The effect of the Revaluation Committee's work was to increase the value of real estate assessed in 1919 by four times the amount assessed in 1915. Further proof of the omission of several thousand acres is shown by the discrepancy between the census of agriculture and the report of the Commissioner of Revenue. These figures have been quoted in part before, and show that the number of acres of land in North Carolina in 1925 was 31,193,600, whereas the Commissioner's report shows an assessment of only 29,824,767 acres. This lays bare the fact that even after the revaluation in 1919 there were still 1,378,833 acres not on the books as late as 1925. An even more convincing fact as to the great degree of looseness in the assessment of land under the present system is the discrepancy in the number of acres assessed from year to year as shown in the report of the Commissioner of Revenue.

Year	*Acres Assessed*
1913	29,314,271
1914	28,432,939
1918	27,926,052
1921	28,021,228
1922	28,888,424
1925	29,824,267
1926	28,453,458

It is unreasonable that the number of acres in a state having constant boundaries should fluctuate by thousands of acres from year to year. If the system were conducted properly, no such large fluctuations would exist, but at present it is evident that thousands of acres are escaping taxation. The revenue lost from such a poor system would pay for the installation of a better one. The revaluation in 1919 cost $130,000 and raised the value of taxable property from $1,009,120,389 to $3,158,480,072—nearly trebled it.[16] There is no doubt but that a more scientific assessment would be welcomed by the people of the state in general, would give more satisfaction, and in the long run would be cheaper.

Assessment of Urban Real Estate

What has been done in the direction of scientific assessment in cities? In the following section will be shown the methods of assessing urban real estate, and later it will be shown how rural real estate could be better assessed by

[15] *Report of the State Tax Commission on Revaluation*. p. 2.
[16] *Wilmington Morning Star*, May 23, 1925.

the application of urban principles. Of course, not all cities are scientifically assessed, but a good many of them are, and the plan which will now be briefly described is the one used by most of them with certain local adaptations. A block and lot map is made of the city. This map shows an outline of the blocks and the lots composing the blocks, the lots being drawn to scale. In addition, it shows the length of all lines bounding the lots. An identification number is placed upon each block and upon each lot within the block. The only other thing necessary is the names of the streets bounding the blocks. If desirable, the width of the streets and the numbers assigned to the lots may also be shown. By this method any lot in the city can be designated by such a description as block 238, lot 31. There would be only one lot which would meet this description. Such a thing as missing land under this system would be almost impossible. After this map has been completed the matter of ownership and dimensions is settled. Next the value must be determined. For this purpose a unit foot is selected. "This is a hypothetical strip of land located at or near the middle of a block, with a frontage of 1 foot and a depth of 100 feet, 120 feet, 140 feet, or 150 feet. The depth in each case depending upon the normal lot depth in the section where the rule is to apply."[17] The strip is taken at the middle of the block because it is possible that its value might be affected by the corners otherwise. After the dimensions for the unit foot have been determined some value must be attached to the unit. This is done by the consideration of rentals and sales records. After the unit land value is decided upon, it is entered on a land value map. This map shows the block boundaries and the block number, also the street lines and names. No property lines are shown. The unit foot value is written along the face of each block. The computation of rectangular lots near the center of the block becomes simple now. It is obtained by multiplying the number of unit feet by the unit foot value. If the lot happens to be over or under the unit foot depth, the value is found by the use of a percentage table which has to be set up. This table shows how much of the value of the lot is contained in the first foot, first 2, 3, 4, 10, 15, 25 feet, and so on back. This table will vary from city to city. In New York two-thirds of the value of a lot is within the half of its depth lying nearest the street; in Cleveland 72.50 per cent of the value is within the first half of the depth. In municipal assessments special consideration must be given irregular lots, off-grade lots, plottage, etc., but as these factors will not be met with in rural assessments, they will not be discussed here. It is important, however, that we consider corner influences, for you have the same kind of a situation when a farm is near a crossroad, market, or something similar. The value is undoubtedly increased and the same is true of a corner lot in the city. Assessors differ in their opinions as to how far inward a corner influences value. In Newark and New Rochelle the first 25 feet are considered to be influenced, or if the corner lot is less than 25 feet, the corner lot alone is considered as having been benefited. In Cleveland and Chicago the first 100 feet are considered to be influenced regardless of lot lines. The determination of the influence is more or less arbitrary. The other

[17]Buck, *Municipal Finance*, p. 348.

problem involves the evaluation of the influence. Both of these problems are met to a less extent in rural real estate assessments.

As has been shown, the matter of assessment in cities is being fairly scientifically conducted. The result is a large degree of uniformity, a fairer valuation for all, and a more complete assessment. The whole secret is a scientific standard. There is no reason why rural real estate assessors should not have standards, and it seems highly probable that most of the principles involved in urban assessments could be employed likewise in rural.

FACTORS INVOLVED IN A SCIENTIFIC ASSESSMENT

Reference has been made in several places to a scientific assessment. What does this involve? First of all, the underlying principle in a scientific assessment is to have records, tables, maps, etc., by which to judge the value of property. These will afford standards by which the assessor can guide himself in making valuations. It is obvious that this would result in a greater degree of uniformity than is obtained by the assessor making a separate guess at the value of each piece of property. The main idea is to have the value worked out by formulas, tables of percentages, and other definite factors which will convert the matter of assessment from a random guess into a scientific study. One of the things which should be obtained by a scientific valuation is an equal standard for all taxpayers, and this should be a 100 per cent valuation. Under the improved method, the assessor would have before him the tax charged John Smith for so many acres of a certain type of land, and when he came to Richard Roe's property, which is identical in nature, he knows he should tax him at the same figure. This degree of fairness would be obtained in the valuation of the entire state. No such thing as the assessing of one farm at 60 per cent of its value and another at 50 per cent should ever happen. Another goal of scientific assessment is to watch the fluctuations in the value of property. The fact that a farm is worth $5,000 now is no reason why it will always be worth that amount. The assessor should be on the watch for property transfers, gather information from sales, and correct his valuations accordingly. One fault of the present system is that the assessor too frequently allows himself to be influenced by the valuation made of the property in previous assessments. The property should at all times be assessed at true value, and any changes in this value should be noted. Where there are no transfers, as in the case of many farms, the value of these can be determined by reasoning from the sales of neighboring farms. By logic and interpolation the value of a piece of property which has not been sold in twenty years can be very accurately obtained.

One of the final things to be considered is the matter of the assessor. If we are to have a scientific assessment, we must have a scientist in the role of assessor. You will have to pay a salary sufficiently high to attract this type of man. You can not leave this office open to incapable men and expect them to value property by formulas and maps with any degree of accuracy. What is needed is a man who knows the theory of taxation and knows how to apply it. The assessor should be a man who understands maps, formulas, and tax

tables, and is capable of making his own maps and tables. Finally, the assessor must be a full-time worker. He should devote his entire time to assessment and should not, as under the present system, work at some trade three-fourths of the year and devote his time to assessment only during the list-taking period. If the valuation is to be fair and equal between farms, the assessor must be at work all of the time, and constantly on the watch for fluctuations in value. Some of the more detailed elements of a scientific assessment have been shown in the section on urban real estate assessment, and will be still further discussed in the section on suggested reforms for the system of assessment in North Carolina.

WHAT OTHER STATES ARE DOING

In discussing rural assessment in North Carolina it is interesting to note the progress that has been made in other states. As has been said before, methods of assessment are, in general, backward throughout the entire United States. A few states have made notable progress, and others are gradually working toward a better system. Several states now make use of assessment maps in the valuation of rural real estate. The board of county commissioners may require the use of these maps in Nevada and Ohio, but in Alabama, California, Iowa, and Oregon their use is compulsory. In New Jersey maps are required for townships having a population in excess of 2,500. The law of Missouri requires the county boards to get plats of all townships in their respective counties from the registrar of the United States Land Office, and to prepare maps for assessors and boards of equalization.[18]

Oregon: Section 4270 of the laws relating to taxation and assessment in Oregon states: "The assessor of each county shall make a plat of the government surveys, . . . and shall note therein, or in a present ownership book or list, the owner of each tract of land, . . . which said plats shall be public records and subject to general inspection."[19]

New Jersey: Article IV, Section 401, 12c, 3, of the New Jersey Tax Laws states: "The Board of Equalization of Taxes may direct the preparation of a tax map, . . . for any township not having a surveyed tax map." Article IV, Section 401, 12J, 1, states: "Hereafter it shall be unnecessary to provide for the preparation of and use of maps for purposes of taxation in townships having a population of less than twenty-five hundred inhabitants." The maps are made from maps of the state geological survey and show highways and streams. The maps are transmitted to the assessors, who indicate on the map the boundaries and area of each parcel of land and designate each parcel by a number or some other mark. The maps are then opened to the criticism of the taxpayers and any necessary corrections are made.

Iowa: Section 7120 of the Revenue Laws of Iowa states: "The County Auditor shall furnish to each assessor a plat book on which shall be platted the lands and lots in his assessment district, showing on each subdivision or part thereof, written in ink or pencil, the name of the owner, the number of

[18] *Report of the Minnesota Tax Commission*, 1926, p. 12.
[19] *Laws Relating to Assessment and Taxation in Oregon*, 1927, p. 11.

acres, or the boundary lines and distance in each, and showing as to each tract the number of acres to be deducted for railway right of way and for roads."

Oregon: The State of Oregon is somewhat ahead of others in that it makes it a requirement that assessors use sales records in making their valuations.

CLASSIFICATION OF LAND

The classification of land is quite common in the United States, three-fifths of the states having adopted the classification of land to some degree.[20]

Louisiana: In Louisiana property is divided into several classes. For example, agricultural lands alone are divided into Classes A, B, and C, the better grade of land being Class A, and so on down. The land is then valued according to the class in which it falls. There is no definite value which must be attached to each acre in each class, but some idea of the value of land in that class is given, and all land is taxed with this value as a base from which to figure. There are also several other classes than agricultural, such as pasture lands and woodlands.

Nevada: Probably the best example of classification is seen in the Nevada system. Land is classified as special, cultivated, wild hay or meadow, pasture, grazing, and mountain or barren. These classes are further subdivided into two to three classes. Each class is definitely described and a certain value is placed upon an acre of land in each. The assessor can not value land in any particular class below the amount specified as the value of an acre of land in that class. However, the assessor may use his judgment as to how high above the amount the land should be valued.[21] This system of classification has a great advantage in that it gives the assessor some base from which to figure values. The objection is that the assessor still has to allocate the land to the various classes, and here he can create inequalities and show favoritism.

SUGGESTED REFORMS IN OTHER STATES

Several other reforms have been suggested in various states by tax commissions or special committees on taxation. These suggestions have not all been enacted as laws, but they show that there is a movement toward reform, and, after all, the agitation of public opinion is the one thing needed to put a measure across. The Efficiency Commission of Kentucky recommended that Kentucky employ farm maps in the assessment of real estate.[22] The Commission expressed the opinion that this would do away with the practice of assessing a different number of acres each year, would create uniformity in assessments, would prevent land from escaping taxation, and would put an end to the practice of returning land at half value and at less than the real area.[23]

A special tax investigating committee in Oregon in 1925 recommended that there be a revision in the salary of assessors commensurate with the work and

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[20] *Report of the West Virginia State Tax Commission*, 1927, p. 181.
[21] *Report of the Nevada Tax Commission*, 1925-1926, p. 19.
[22] *Report of the Efficiency Commission of Kentucky*, 1924, p. 316.
[23] *Ibid.*, 1924, p. 265.

responsibilities involved.[24] This is a worth-while idea and should be given more consideration in other states. Many faults of the present system of assessment in several states can be attributed to incapable assessors, and until more is paid assessors capable men can not be employed.

Suggested Reforms for the System in North Carolina

North Carolina has not kept pace with some of these states and, on the other hand, it is highly probable that there are other states that are behind North Carolina. There is no doubt but that there is room for much improvement in the system in this state, and that these improvements should be made. A brief discussion will now be made of proposed reforms for North Carolina.

Sources for Determining Values

One of the most important reforms would be the abolition of the arbitrary, guess-work method of establishing values. There are several sources that the assessor could use in determining the value of the land he is assessing. One of the most important of these is the record made in the register of deed's office of sales and transfers of property. This source is extremely valuable and should be much used by the assessor. Here he is able to find at exactly what price land is being sold, and by reasoning and interpolation he is able to determine the value of property that has not been transferred by using the figures found in the case of transferred lands. There are two things involved here. The assessor must discard figures of unusual or forced sales. They are not representative of actual value and consequently could not be used. Furthermore, deeds, records of sales, etc., should and must contain the actual considerations of the sale. The full amount paid for the property should be shown on record. In order to provide for this as an assistance to assessors, there should be a law passed to require the recording of the true consideration for which property is sold. There is no worthy reason why the true consideration should be withheld, and so long as we continue to assess property at its "true value in money," the term being construed to mean the value of property when sold as property is usually sold, the actual amounts transferred should appear in the record of the transfer.

A second reform which should take place is concerned with the assessor. Most states now agree that his territory should be the county. Township assessors have a tendency to create greater inequalities. Then, too, the counties are the fundamental units into which the state is divided and it is therefore best to have them as the assessment districts. The assessor should be paid a higher salary. This would cause more capable men to become interested in the work. One requirement of any man desiring to become an assessor should be that he pass a civil service examination. This examination is given applicants for such positions as mail carriers and various governmental positions, and there is no reason why assessors should not meet the same requirement. It would eliminate most of the incapable and inefficient applicants. Some central authority, perhaps the board of commissioners, should appoint the assessors

[24] *Special Tax Investigating Committee of Oregon*, 1925, p. 21.

from those who pass the examination. They should be appointed by a central authority for two reasons:

(1) Assessing is essentially technical work and the populace as a whole is incapable of electing an assessor. The public in general does not understand the work.

(2) An assessor who is thus appointed would not be responsible to the voters for his office, and consequently would not be as likely to be influenced by political and external forces.

As a final recommendation as to the assessor, I would suggest that he be subject to recall by a majority vote of the voters. This may seem contradictory in that I have said that the people are incapable of electing him. The point to bear in mind is that the assessor is an agent of the public, working for the public, and paid by the public, and as such should satisfy the majority of the members who make up the public. Although the people are incapable of electing him, they nevertheless know when they are pleased, and in the few cases in which they would want to use the power of recall I think that they should be allowed to do so. Then, too, as a further argument, the power of recall would serve as a partial check upon any negligence upon the part of the board of commissioners.

Probably one of the greatest steps that could be taken toward the improvement of assessment in North Carolina would be to prepare assessment maps. These maps are now used in a number of states and have proven a great aid in land valuation. In Nevada and Ohio the use of such maps is optional, but in Alabama, California, Iowa, and Oregon the use of assessment maps is compulsory. Such maps when prepared should show the boundaries of each farm and the number of acres in the farm. The land should be classified and the map should show the number of acres in each class. The matter of determining the classes of land is a more or less optional one. Some states use only four or five classes, such as tillable, swamp, timber, stony, waste, etc. Other states go further and subdivide these classes into Class A, tillable; Class B, tillable; and so on. The numbers and names of the classes are more or less determined by the nature of the land in a particular state. When the boundaries of the farm, the classes of land, and the number of acres in each class are shown it now remains to draw in highways, railways, bodies of water, and any other factors that would influence the value of the land. It stands to reason that nearness to a highway, market, or railroad would affect the value of the property and should be taken into consideration in assessing it. When all of these things are shown on the map it is practically complete as far as assessment purposes are concerned. The only thing remaining to be done is to designate each farm by a particular number. This number is identical with one carried on a card index, the use and preparation of which will be discussed later.

There are two ways in which these assessment maps may be prepared. One is by the ordinary method of survey used in the preparation of blue prints, determining farm boundaries, and the preparation of maps. The second method of making tax maps is aerial photography. The first method is

generally understood, but the second has come into prominence recently and has not been generally used. As the name implies, an aerial photograph is a picture of the property taken from the air. These pictures are taken in such a way and at such a height that the contract prints from the negative show a definite scale. The size of the picture and the scale can be adjusted to suit the use made of the maps. After the photographs have been made, property lines and the like can be drawn in to complete the assessment maps. There are several advantages that the aerial photography method has over the old practice of land surveying. The new method is less expensive, quicker, and shows with absolute fidelity the facts concerning the property. The nature of every strip of land and the surrounding highways, bodies of water, etc., are shown. It would be almost impossible to omit any land. Aerial photography has been rarely used in rural areas, and it is therefore necessary to draw illustrations from urban uses. The following results were found from the use of this method in Middletown, Connecticut: 1,896 pieces of property had been omitted from previous assessments; 223 dwellings were found which had been escaping taxation; 1,351 barns, sheds, and private garages were discovered; and 111 stores, shops, and public garages were found. As a result of these findings, the grand list in Middletown was raised from $20,500,000 to $31,500,000, and the tax rate was lowered from $30 to $24 per thousand. In East Haven, Connecticut, similar findings lowered the rate from $28.80 to $15 per thousand. In Manchester the rate was lowered from $18 to $12. It was also found by a study in this same state that it took four years to make a map of New Britain at a cost of $60,000 by the old survey method; and it took only 60 days at a cost of $7,000 to make a map of Middletown by means of aerial photographs. New Britain has an area of 13 square miles, while the area of Middletown is 43 square miles.[25] In an article in the National Municipal Review, S. M. Fairchild says, "There is no questioning the fact that the recordation of ground detail by means of aerial photographs markedly surpasses the older method in accuracy, speed, and cost."[26] As a further reform, I would suggest that these maps, when completed, be posted in a public place for criticism by the taxpayers.

When the completion of the maps has taken place, index cards should be prepared for use in connection with the assessment maps. This is known as the card index system, to which reference was made in a previous paragraph. One card is made for each farm and bears a number corresponding to the number of the farm upon the map. The name of the farm owner is written upon the card along with a description of the location of the property. Following this are listed the number of acres in each class of land and the value per acre. These figures are then multiplied, added, and the total value of the property shown. At the bottom of the card is left a space in which the assessor can write any remarks he cares to make. The method of determining the value per acre varies in different states. Some leave the valuation entirely in the hands of the assessor. Others place limits within which the assessor is to

[25] *Minnesota Tax Commission Report*, 1926, p. 112.

[26] Fairchild, "Aerial Photographs Aid Tax Assessors," *National Municipal Review* July, 1926.

decide. I think that the best plan is to have the person hired as a full-time supervisor for the county determine the value of land per acre by the use of sales records and other sources that may be available. Then let him submit to the board of county commissioners and the state board of equalization an upper and lower limit within which he thinks the various classes should be valued. If the limits are approved by the two boards, they could then be turned over to the assessors for their use. If, because of unusual conditions, the assessor finds it necessary to use the lower limit or the upper limit or even to go outside of the limits, he could state his reasons in the space at the bottom of the index card.

It is not claimed that exact equality as between taxpayers will result from the use of maps and cards, but it is certainly true that there are several advantages to be had from it. These tools will afford the assessor a convenient method of comparing values. He has a standard to guide him in valuing two pieces of property in different sections of the township. By the use of maps he is enabled to reduce the degree of discrimination to a great extent. Greater relative equality is obtained between property owners because of the easy manner in which inequalities are discerned. Aside from the assessor, the taxpayer is also benefited, because he is better able to compare the assessed value of other property in his locality.

SUMMARY

In this paper an attempt has been made to show the importance of rural real estate in our taxation system, the need for accuracy in assessments, and the weaknesses that exist in the taxation system of North Carolina. In view of these weaknesses, several reforms have been suggested. It is regrettable that so many illustrations and figures had to be taken from other states, but the lack of study of taxation in North Carolina and the lack of compiled facts and figures dealing with the taxation question have made this necessary. It is to be hoped that interest in taxation in this state will be stimulated, and that in the near future rapid strides may be made in the improvement of our system.

THE TAXING OF INTANGIBLE PERSONAL PROPERTY

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(Report made to State Tax Commission and reprinted with the permission of Dr. Keister and the Commission)

Intangible personal property is commonly thought of as including shares of stock, bonds, notes and accounts receivable, mortgages, and bank deposits. In addition to these, business firms may possess intangible property in the form of good-will, trade marks, patents, etc. This report deals with intangibles of the first group mentioned, since it is these that present the most difficult problems of intangible property taxation. Business intangibles of the second type, good-will and the like, when owned by corporations, are assessed in this state by entirely different methods from those used with the first type, i.e., by the State Board of Assessment through the corporate excess tax.

There are three questions to be considered in this problem of the taxation of intangibles. They are:

I. What is the present situation?
II. Why is the present situation unsatisfactory?
III. What may be done?

These questions will be discussed in the order named.

I. What is the Present Situation?

There are five principal facts to be known about the present situation. They are:

1. What is the amount of intangibles listed for taxation in the state?
2. What kind of intangibles are listed?
3. By whom are intangibles listed?
4. What significant differences are found among counties and townships?
5. How much revenue are we getting from intangibles at present?

1. *What is the Amount of Intangibles Listed in the State?* The first aspect of the present situation to be inquired into is the amount of intangible property listed for taxation in the state. It is important to know whether this amount has been increasing or decreasing in recent years. The facts are shown in Table 1. In taxation parlance, intangibles are called solvent credits in this state. We do not require shares of stock of either domestic or foreign corporations to be listed. Debts may be deducted from credits to get net or taxable solvent credits.

TABLE I. SOLVENT CREDITS LISTED FOR TAXATION IN THE STATE, 1921-1927
(Sources—Annual Report of the Commissioner of Revenue and Population Estimates of the United States Bureau of the Census.)

Fiscal year ending June 30	Amount in thousands of dollars	Amount per Capita	Percentage of total property assessed
1921	192,829*	73.77	7.5
1922	185,939*	70.17	7.2
1923	167,010	62.18	6.3
1924	167,624	61.56	6.2
1925	162,405	57.75	5.9
1926	164,026	57.38	5.8
1927	150,469	51.94	5.2

*Excluding stock in foreign corporations which was subject to taxation until 1923.

During the seven years intangibles on the tax books have declined both in absolute amount and in relation to other property. In absolute amount listed intangibles declined 22 per cent in this period, while their ratio to total property in the state declined from 7.5 per cent to 5.2 per cent. The per capita amount declined from $73.77 to $51.94. This looks suspicious. It is difficult to believe that the actual amount of taxable intangibles in the state declined at all during these seven years. On the contrary, in view of the industrial and commercial development of the state, there is every reason to think that it increased. We have no reliable estimates of the growth of wealth or of income in the state for these years. However, we may compare our listed intangibles with the growth of our bank deposits, since bank deposits are considered a good index of the financial growth of a state. The following table shows the contrast between these two items:

TABLE 2. LISTED INTANGIBLES COMPARED WITH BANK DEPOSITS IN NORTH CAROLINA, 1921-1927

(Sources—Annual Reports of Commissioner of Revenue and of the Comptroller of the Currency)

Fiscal year	Amount of listed solvent credits, in thousands of dollars	Percentage of Decrease— Based on 1921	Amount of bank deposits in thousands of dollars	Percentage of increase+ Based on 1921
1921	192,829		252,139	+ .....
1922	185,939	— 3.57	275,631	+ 9.32
1923	167,010	—13.39	299,623	+18.83
1924	167,624	—13.07	313,100	+24.18
1925	162,405	—15.78	318,353	+26.26
1926	164,006	—14.95	352,767	+39.91
1927	150,469	—21.97	356,767	+41.50

Bank deposits—which, by the way, are supposed to be listed for taxation by the depositor in his solvent credits—started out by exceeding the solvent credits by 31 per cent and ended up by exceeding them 137 per cent.

While bank deposits were increasing 41 per cent, intangibles listed were decreasing 22 per cent. Apparently the better off we become the less likely we are to admit it.

An even better index of the probable growth of wealth and income in the state may be constructed by averaging the growth of state income taxes paid, automobile licenses, gasoline taxes, and bank deposits. Taking 1922 figures as a base, the amount in subsequent years is expressed as a percentage of the 1922 amount, after adjusting the figure to eliminate the effect of an increase in tax rates.[1]

[1]In 1925 the income tax rates were raised approximately 40 per cent; in March, 1923, the gasoline tax was increased from 1 cent to 3 cents and in May, 1925, was made 4 cents. No significant change has been made in the automobile license rates since 1921.

TABLE 3. GROWTH OF WEALTH AND INCOME, MEASURED BY CERTAIN TAXES PAID AND BANK DEPOSITS, COMPARED WITH ASSESSED SOLVENT CREDITS.

	State income taxes paid	State automobile licenses paid	State gasoline taxes paid	Bank deposits in state	Mean average of four preceding indices	Assessed solvent credits
1922 index	100	100	100	100	100	100
1923 index, after adjustment eliminating effect of increased rates	135	122	102	109	117	90
1924 index adjusted	169	164	158	114	151	90
1925 index adjusted	142	195	199	116	163	87
1926 index adjusted	164	219	206	128	179	88
1927 index adjusted	171	243	242	129	196	81

According to this index, admittedly a rough approximation which probably overstates the growth of the state, our economic ability increased 96 per cent while our assessed intangibles fell off 19 per cent. All of the indices of ability showed increases, whereas intangibles decreased.

Another way to judge whether or not we are listing a reasonable percentage of all solvent credits in the state is to compare our total with that listed in neighboring states. Most of our neighboring states do not publish figures that may be compared with ours. However, from the reports of Virginia and Kentucky some comparable figures may be obtained. The facts are shown in Table 4 (estimates of wealth and population taken from United States Bureau of the Census, assessed intangibles from state reports).

TABLE 4. WEALTH AND ASSESSED INTANGIBLES IN NORTH CAROLINA, VIRGINIA, AND KENTUCKY

	North Carolina	Virginia	Kentucky
Total wealth, 1922	$4,543,110,000	$4,891,570,000	$3,582,391,000
Per capita wealth, 1922	1,703	2,050	1,459
Assessed intangibles, 1926	164,006,000*	368,654,000**	792,771,000***
Per capita assessed intangibles, 1926	57.38	159.64	353.48****

From the foregoing table it appears that whereas we have somewhat more wealth than Kentucky, and less than Virginia, we fall considerably below Virginia and far below Kentucky in the amount of intangibles on our tax books. It should be remembered in this connection that both Virginia and Kentucky classify intangibles and apply a low rate to them. Naturally this encourages listing. It should also be noted that Kentucky taxes bank deposits at the source—that is, against the bank—thereby getting practically all

*Law permits deduction of debts from gross solvent credits listed.

**In order to make a comparison, this figure includes, as nearly as may be computed, only the items which are taxable under North Carolina laws. Debts not deductible under Virginia laws.

***Includes, in addition to items taxed in North Carolina, stock in foreign corporations. Reports do not permit separation of this item.

****If bank deposits, taxed against the bank, were omitted, the amount would be $189.44 per capita.

deposits on the tax books. Of the 793 millions of intangibles assessed in Kentucky in 1926, 335 millions were bank deposits. Whether the causes for the above showing lie in low rates of taxation on this class of property, or in taxing certain intangibles at the source, or in something else, the fact remains that we are considerably behind these other states in placing intangible property on the tax books.

2. *What Kinds of Intangibles Are Listed?* After discovering how much intangible property is listed for taxation, our next inquiry is: what kind of intangible property is listed? Are our taxpayers listing chiefly bonds or bank deposits? What proportion of the total consists of notes and mortgages?

The annual reports of the State Commissioner of Revenue do not answer these questions because the reports of county auditors to the State Department of Revenue do not itemize solvent credits. To answer these questions it was necessary, therefore, to go to the county records in representative counties and get the facts from the abstracts filed by the taxpayers themselves. Twenty counties were selected in different parts of the state and in these counties every twenty-fifth abstract was copied.[2] This gave a small but possibly a fair sample of the county. From this sample it appears that the distribution of the different kinds of intangibles is as follows:

TABLE 5. KINDS OF INTANGIBLES LISTED IN DIFFERENT REGIONS OF THE STATE, EXPRESSED AS PERCENTAGE OF THE TOTAL

	Tidewater	Coastal Plain	Piedmont	Mountain	For the state as a whole
Bonds	0.2	0.6	2.3	5.0	2.3
Bank deposits	25.3	20.9	17.6	18.0	18.7
Notes and mortgages	39.9	56.0	52.0	56.7	53.6
Accounts receivable	34.6	22.5	28.1	20.3	25.4
Total	100.0	100.0	100.0	100.0	100.0

From this table it appears that our taxpayers list practically no bonds anywhere in the state. Bank deposits account for about one-fourth of the total intangibles in the Tidewater region, one-fifth in the Coastal Plain, one-sixth in the Piedmont, and almost one-fifth in the Mountain region. Incidentally, it may be noted that if 18.7 per cent of the intangibles are bank deposits, it means that $28,138,000 of bank deposits are listed throughout the state. This is eight per cent of the total bank deposits in the state. Notes and mortgages account for the largest share of intangibles in all regions, representing about two-fifths of the total in the Tidewater, and over half in the Coastal Plain, Piedmont, and Mountain regions. Book accounts and claims are of considerable importance, varying from one-fifth of the total in the Mountain to one-third of

[2]The twenty counties were, by regions:

Tidewater	*Coastal Plain*	*Piedmont*	*Mountain*
Pasquotank	Wake	Guilford	Wilkes
Craven	Johnston	Person	Burke
New Hanover	Pitt	Yadkin	McDowell
Pender	Wilson	Cleveland	Buncombe
	Scotland	Mecklenburg	
	Richmond		
	Vance		

the total in the Tidewater region. Doubtless the chief reasons why notes and mortgages predominate so strongly are these: first, notes are not collectible at law unless listed for taxation; second, mortgages listed for taxes may be checked against those recorded in the county. Some counties do so and thereby add appreciable amounts of solvent credits to the roll. All of which suggests that unless there is a direct incentive to list intangibles, relatively few of them will be listed.

3. *By Whom Are Intangibles Listed?* Another set of queries relates to the persons listing intangibles. How many persons list such property? Do as many country people list intangibles as town people, in proportion to their numbers? To what extent do corporations account for our solvent credits? Here again for an answer we are compelled to go back to the county records. In sixteen counties the total number of persons listing intangibles was counted; the total number of persons listing any kind of property was also counted. This was approximately the total number of taxpayers in the county, and the amount of solvent credits listed was recorded. The results are given in Table 6.

TABLE 6. NUMBER LISTING INTANGIBLES IN REPRESENTATIVE COUNTIES OF THE STATE IN 1927

County	Number listing net solvent credits	Amount net solvent credits listed	Average amount per person listing	Total number listing property of any kind	Percentage listing solvent credits of total number
Craven	309	796,072	2,576	12,615	2.4
Pender	292	168,001	575	6,125	4.8
Pasquotank	495	1,040,356	2,102	6,473	7.6
Scotland	213	1,663,306	7,808	5,777	3.7
Richmond	316	1,021,256	3,232	10,405	3.0
Pitt	1,273	2,400,350	1,886	16,233	7.8
Johnston	2,154	2,601,624	1,208	18,627	11.6
Vance	541	1,636,370	3,025	7,141	7.6
Wake	1,649	3,128,006	1,897	33,489	4.9
Mecklenburg	3,225	9,648,041	2,992	26,202	12.3
Rowan	1,751	2,474,631	1,413	15,689	11.2
Guilford	3,391	7,708,143	2,273	42,201	8.0
Person	483	638,439	1,322	4,996	9.7
Yadkin	1,168	1,025,187	878	5,167	22.6
McDowell	418	653,352	1,563	6,311	6.6
Buncombe	3,049	8,626,933	2,829	29,142	10.5
	20,727	45,229,967	2,182	246,593	8.4

The foregoing table shows that in these sixteen typical counties, containing over 240,000 taxpayers, only 20,727 persons, including corporations, admit they own net solvent credits. One out of every 12 taxpayers in these counties so lists. Taking the average amount listed per person in these counties, $2,182, and dividing it into the total amount listed in the state, $150,469,000, it would appear that only 69,150 citizens, including corporations, listed taxable intangibles in North Carolina.

To what extent are country folk represented among those listing intangibles? One might suppose that few farmers own intangibles, since their capital is, in many cases, entirely absorbed by the farm. Towns and cities are usually thought of as the home of intangibles. In the towns are found the business firms, many of which possess intangibles. The towns also claim many persons

who are saving money but do not have any business of their own in which to invest. To discover to what extent country and town people were listing intangibles, the condition of the county records made necessary certain assumptions. We had to assume that all the people living in a township in in which a city lay were town people and that all the people living in townships outside large towns were country people. For example, it was assumed that all the people living in Greenville township were city people and that all people in Pitt County outside of Greenville township were country people. The errors in these two assumptions may offset each other. Some Greenville township residents do not live in the city of Greenville, but their number may well be offset by those in country townships who live in small towns, such as Ayden. If these errors do not offset each other, the results are inaccurate to that extent. The figures for ten counties are shown in Table 7.

TABLE 7. LISTING OF INTANGIBLES BY TOWN AND COUNTRY PEOPLE RESPECTIVELY IN TEN REPRESENTATIVE COUNTIES FOR 1927

Territory	No. of individuals (white and colored) listing solvent credits	No. of individuals listing property of any kind	Percentage listing solvent credits of those listing property of any kind	Amount of solvent credits listed	Percentage of total amount in county	Average amount per person listing solvent credits
1. Charlotte Township	1,785	16,897	10.6	3,277,725	72.6	1,836.26
Mecklenburg County outside Charlotte Township	1,183	9,305	12.7	1,234,253	27.4	1,043.33
2. Marion and Old Fort	284	4,354	6.5	540,423	82.7	1,902.90
McDowell County outside Marion and Old Fort townships	134	1,957	6.8	112,929	17.3	842.75
3. Rockingham Township	81	2,749	2.9	117,608	33.1	1,451.95
Richmond County outside Rockingham Township	206	7,494	2.7	237,300	66.9	1,151.94
4. Elizabeth City Township	246	3,461	7.1	507,168	55.6	2,061.66
Pasquotank County outside of Elizabeth City	238	2,972	8.0	404,295	44.4	1,698.72
5. New Bern Township	214	5,745	3.7	701,375	88.1	3,277.45
Craven County outside of New Bern Township	95	6,870	1.4	94,697	11.9	996.81
6. Greenville Township	205	3,895	5.3	537,315	22.4	2,621.05
Pitt County outside of Greenville Township	1,068	12,408	8.6	1,863,035	77.6	1,744.41
7. Greensboro and High Point townships	2,096	32,122	6.5	3,657,462	68.7	1,744.97
Guilford County outside of Greensboro and High Point	1,295	10,079	12.8	1,664,829	31.3	1,285.58
8. Asheville Township	1,581	16,876	9.4	6,151,510	71.3	3,890.90
Buncombe County outside of Asheville Township	1,468	12,266	12.0	2,475,423	28.7	1,686.26
9. Raleigh Township	340	14,263	2.4	674,502	32.6	1,983.83
Wake County outside of Raleigh	1,234	18,276	6.8	1,395,775	67.4	1,131.10
10. Salisbury Township	606	6,068	10.0	1,013,984	41.0	1,673.24
Rowan County outside Salisbury	1,145	9,621	11.9	1,460,647	59.0	1,275.67
Total city townships	7,438	106,430	7.0	17,179,072	61.1	2,309.64
Total county townships outside of city townships	8,066	91,248	8.8	10,943,185	38.9	1,356.70

Judging by the data in Table 7, country people, in proportion to their numbers, list intangibles more faithfully than city people, although the average amount declared by city people is larger. In the rural townships of these 10 counties, 8.8 per cent of the taxpayers list solvent credits, whereas in the city townships only 7 per cent so list. Of the total amount of intangibles listed by individuals in these 10 counties, 61 per cent was listed by city people, 39 per cent by rural people. Apparently, business firms domiciled in the cities helped to raise the average for the cities.

To what extent do corporations account for our solvent credits listed? It is impossible to answer this question accurately because many of the counties do not keep their corporation tax listings separate from those of individuals. A questionnaire sent to county auditors asking for the amount of net solvent credits and of real estate listed by corporations and individuals, respectively, brought returns as shown in Table 8.

TABLE 8. SOLVENT CREDITS IN RELATION TO REAL ESTATE LISTED BY CORPORATIONS AND INDIVIDUALS IN CERTAIN COUNTIES, 1927

County	Solvent credits listed by individuals	Solvent credits listed by corporations*	Real estate listed by individuals	Real estate listed by corporations	Percentage corporation solvent credits are of total solvent credits	Percentage corporation real estate is of total real estate
Alamance	$ 1,452,996	$ 271,772	$19,243,230	$ 3,412,461	15.8	15.1
Avery	155,407	123,087	3,904,257	796,663	44.2	16.9
Cleveland	1,681,927	125,958	21,457,263	6,251,642	7.0	22.6
Cumberland	625,676	153,856	17,898,861	2,907,296	19.7	14.0
Davidson	1,626,426	1,023,977	18,058,397	6,180,714	38.6	25.5
Granville	782,760	117,592	10,894,935	1,003,920	13.1	8.4
Halifax	1,231,724	115,658	17,565,365	7,219,403	8.6	29.1
Iredell	1,617,600	658,831	24,459,181	5,710,384	28.9	18.9
Jackson	357,579	891,180	5,647,557	94,870	71.4	1.7
Mecklenburg	4,511,990	5,136.060	88,003,040	24,267,796	53.2	21.6
New Hanover	1,076,093	318,455	37,316,880	9,369,395	22.8	20.1
Richmond	358,198	666,348	14,908,462	9,230.265	65.0	38.2
Rutherford	1,216,574	109,656	15,299,772	10,073.970	8.3	39.7
Wayne	1,895,257	292,827	32,767,005	2,207,954	13.4	6.3
Total	$18,590,207	$10,005,257	$327,434,205	$88,726,733	35.0	21.3

*Not including railroads and other public service corporations assessed by the State Board of Assessment.

Assuming that these counties are typical of the state as a whole, it appears that corporations list 35 per cent of all solvent credits listed in the state, whereas they own only 21.3 per cent of all the real estate. In two mountain counties, Avery and Jackson, the ratio of corporate to total solvent credits is above average, as it is in Mecklenburg, Richmond, and Davidson counties. In other words, both non-industrial and industrial counties are found among those above average. If this sample is representative (it should be noted that no Tidewater counties are included), it indicates that more than one-third of all the solvent credits listed in the state are listed by corporations.

It is important also to know what percentage of all corporations lists intangibles and in what average amount. Among the counties visited by the

Commission's investigators, those in the following table segregated the corporation tax abstracts in such a way as to make a sampling possible. Accordingly, every tenth corporation abstract was copied in these counties. The results are shown in Table 9.

TABLE 9. NUMBER OF CORPORATIONS LISTING INTANGIBLES AND AMOUNT LISTED, 1927
(Data from sample records in the counties)

County	No. of corporation lists copied (every tenth one on file)	Number of these listing gross solvent credits	Number listing net solvent credits	Amount of net solvent credits listed by those in preceding column	Average amount net solvent credits listed
Burke	10	1	1	20,652	20,652
Guilford	58	30	10	153,811	15,381
Mecklenburg	33	26	11	120,553	10,959
New Hanover	26	6	2	690	345
Pasquotank	5	4	1	300	300
Richmond	10	3	3	1,709	570
Vance	8				
Wake	46	17	9	101,550	11,283
Wilson	12	8	4	154,034	38,509
Total	208	95	41	553,299	13,495

The 208 corporation records on which the table is based may be too small a sample from which to draw conclusions. It suggests that almost half (46 per cent) of our corporations list gross solvent credits, that 20 per cent of all list net solvent credits, and that the average amount listed is $13,495. These figures may be compared with corresponding data of all taxpayers. It will be remembered that only 1 in 12 of all taxpayers, including corporations, listed net solvent credits in the 16 counties shown in Table 6. This compares with 1 in 5 corporations in the 9 counties of this table. The average amount for all taxpayers, including corporations, in the 16 counties (Table 6) was $2,182 compared to $13,495 for corporations alone in the small sample of Table 9. It is possible that corporation officials are more honest in listing intangible property than individuals are. It is possible that corporations really own 6 or 7 times as much intangible property per corporation as the average for individuals and corporations combined. It is also possible that corporations list intangibles more faithfully than private indviduals do, merely because they believe they will be taxed on their intangibles through the corporate excess tax if they do not list them with the local assessors. Whatever the explanation, the figures in both Table 8 and Table 9 seem to point to the fact that corporations are responsible for placing large amounts of intangibles on the tax books.

4. *What Significant Differences Are Found Among Counties and Townships?* To what extent does uniformity prevail among the counties and townships in getting intangibles on the books? Are some counties much more successful in administering the law than others? We may expect to find certain counties showing a greater amount of intangibles than others, as some counties are

much wealthier than others. The percentage of solvent credits to total property is a much fairer test than the absolute amount. In the following table, which includes all the counties of the state, the number of counties listing the various percentages of solvent credits to total property is shown.

TABLE 10. NUMBER OF COUNTIES LISTING VARIOUS PERCENTAGES OF SOLVENT CREDITS TO TOTAL PROPERTY IN 1927
(Data from reports filed with Commissioner of Revenue)

Percentage of solvent credits to total real and personal property in the county (Average for all counties, 5.7)	Number of counties
0 to .9	2
1 to 1.9	3
2 to 2.9	9
3 to 3.9	17
4 to 4.9	18
5 to 5.9	19
6 to 6.9	11
7 to 7.9	8
8 to 8.9	6
9 to 9.9	2
10 to 10.9	2
11 to 11.9	0
12 to 12.9	2
13 to 13.9	1

It is evident from this table that a few counties list practically no solvent credits. The five lowest counties are all Tidewater counties (Dare, Pamlico, Brunswick, Carteret, and Washington). On the other hand, several show a gratifying result—12 per cent or over (Stokes, Forsyth, and Scotland). The heavy bunching occurs between 3 and 7 per cent, 65 of the 100 counties lying in these four percentage groups.

It is enlightening to compare one county with another of substantially similar economic standing, preferably an adjoining county of about the same size and amount of wealth. Such a comparison is made in Table 11. Pairs of adjoining counties, quite similar in economic conditions, show some marked contrasts in their listing of intangibles. Since the willingness of individuals to list their intangibles is commonly supposed to vary inversely with the tax rate (the higher the rate, the less willingness), the tax rates are also given in the table.

TABLE 11. INTANGIBLES LISTED IN ADJOINING COUNTIES, 1927, WITH TAX RATES FOR 1926
(Data from county abstracts and reports of Commissioner of Revenue)

County	Amount of assessed solvent credits (in thousands of) dollars)	Percentage solvent credits are of total real and personal property in county (average for state =5.7 per cent)	County tax rate for 1926 per $100
Nash	$ 2,348	7.7	$ 1.35
Edgecombe	1,084	3.5	1.08
Scotland	1,663	12.0	1.35
Robeson	874	2.8	1.20
Forsyth	24,284	12.7	.55
Guilford	7,790	4.3	1.10
Northampton	1,091	9.6	1.10
Halifax	1,347	4.0	1.50
Vance	1,771	10.2	1.50
Granville	900	5.9	1.58
Yadkin	965	10.5	1.50
Davie	781	6.6	1.40
Davidson	2,661	8.1	1.25
Rowan	2,475	3.9	1.07
Johnston	2,602	7.0	1.79
Harnett	664	3.0	2.00
Stokes	1,608	13.2	1.67
Rockingham	1,810	4.6	1.69
Bertie	1,201	8.9	1.70
Washington	124	1.6	1.65

The percentage of solvent credits to total property in the county (column 2) is more significant than the actual amount listed (column 1). These percentages show striking variations between neighboring counties. Forsyth, for example, shows three times as high a percentage as Guilford, Scotland over four times as high a percentage as Robeson, and Bertie five and one-half times as high as Washington. The tax rate seems to have little to do with the result in these ten pairs of counties, since in five of the ten a higher percentage of solvent credits is assessed in the county with the higher rate.

Another bit of evidence regarding the efficiency of different counties in getting intangibles on the books may be seen in the number listing solvent credits compared with the total number listing property of any kind.[3]

TABLE 12. NUMBER LISTING SOLVENT CREDITS COMPARED WITH TOTAL NUMBER ON THE TAX BOOKS IN REPRESENTATIVE COUNTIES IN 1927
(Fractions expressed in nearest whole number. Data taken from county scrolls)

County	Out of every 100 persons listing property, the number listing solvent credits is
Buncombe	10
Burke	12
Cleveland	15
Craven	2
Guilford	8
Johnston	12
Mecklenburg	12
McDowell	7
Pasquotank	8
Pender	5
Person	10
Pitt	8
Richmond	3
Rowan	11
Scotland	4
Vance	8
Wake	5
Wilkes	16
Yadkin	23
Average for all 19 counties	9

From Table 12 it appears that some counties are much more successful in getting taxpayers to list solvent credits than other counties are. One should not expect to find counties equal in this respect. Yet the differences shown in the table seem too great to be explained on the basis of differences in the amount actually owned. The highest county shows ten times as many listings per 100 taxpayers as the lowest county. The three lowest show four or fewer per 100, while the three highest show 15 or more per 100. Strictly rural counties are found among the lowest and among the highest. The same is true of counties containing large cities.

The conclusion seems inescapable that certain counties are much more diligent in seeking and finding intangibles than others.

Among townships within the same counties even more striking differences appear. The counties analyzed in Table 13 were selected, not through any desire to expose their particular shortcomings, but because they are believed to be typical.

[3]This number is almost, but not exactly, the same as the total number of taxpayers in the county. If a man owns property in two townships, his name will appear twice on the county scrolls. Little error is involved, however, in assuming that the number listing property of any kind is the number of taxpayers.

TABLE 13. SOLVENT CREDITS BY TOWNSHIPS IN REPRESENTATIVE COUNTIES IN 1927

(Data from county records)

Township	Total solvent credits	Total real estate	Percentage solvent credits are of real estate	Out of every 100 persons listing property the number listing solvent credits is:	Among those listing solvent credits the average amount listed is:
McDowell County					
Marion	$ 446,501	$ 5,906,243	7.6	6	$2,157
Old Fort	93,922	1,042,526	9.0	9	1,219
Nebo	37,687	1,442,573	2.6	11	1,018
Glenwood	21,275	196,869	10.8	11	851
Montford Cove	9,028	218,849	4.1	9	502
Higgins	2,585	78,565	3.3	8	323
North Cove	21,989	494,911	4.4	4	846
Dysartville	20,365	250,108	8.1	6	1,018
Bracketts	.....	65,549	.....	.....	.....
Crooked Creek	24,608	224,544	11.0	8	946
Guilford County					
Gilmer	1,940,263	40,167,959	4.8	10	2,200
Morehead	2,793,120	50,906,073	5.5	6	4,002
High Point	1,136,065	38,340,552	3.0	4	2,202
Bruce	75,038	1,035,241	7.3	10	1,172
Deep River	131,520	1,059,778	12.4	17	1,342
Friendship	195,906	1,776,124	11.0	12	1,531
Greene	95,214	689,623	13.8	19	1,107
Jamestown	329,584	2,698,364	12.2	8	3.544
Oak Ridge	132,664	1,252,698	10.6	11	1,525
Fentress	103,276	1,379,053	7.5	14	1.033
Clay	154,237	870,615	17.7	19	1,455
Monroe	90,733	1,266,464	7.2	11	1,019
Rock Creek	119,888	2,450,396	4.9	9	1,347
Sumner	83,490	1,098,245	7.6	13	861
Washington	102,900	682,172	15.1	21	1,143
Center Grove	63,780	843,606	7.6	12	1,063
Jefferson	160,465	1,076,214	14.9	17	1,486
Johnston County					
Selma	65,881	2,982,314	2.2	4	1,014
Smithfield	502,268	4,380,529	11.5	10	2,025
Bentonsville	59,544	756,773	7.9	13	805
Pleasant Grove	84,626	809,064	10.5	19	694
Meadow	94,296	1,129,567	8.3	15	742
Ingrahams	160,352	1,594,051	10.1	16	663
Elevation	158,634	1,416,532	11.2	20	1,023
Cleveland	89,340	842,399	10.6	10	1,942
Pine Level	164,608	843,685	19.5	7	4,703
Clayton	534,192	3,275,030	16.3	10	3,124
Wilders	49,946	1,781,445	2.8	5	1,086
Micro	62,777	817,040	7.7	6	1,902
Oneals	103,047	1,941,673	5.3	8	1,000
Wilson's Mills	71,858	707,430	10.2	8	2,566
Beulah	87,395	1,811,861	4.8	17	802
Boon Hill	92,361	1,917,719	4.8	30	246
Banner	220,499	2,402,042	9.2	12	1,267

TABLE 13 (*Continued*). SOLVENT CREDITS BY TOWNSHIPS IN REPRESENTATIVE COUNTIES IN 1927

(Data from county records)

Township	Total solvent credits	Total real estate	Percentage solvent credits are of real estate	Out of every 100 persons listing property the number listing solvent credits is:	Among those listing solvent credits the average amount listed is:
Pender County					
Holly	$23,451	$ 466,664	5.0	4	$1,172
Long Creek	130	403,674	0.03	0.2	130
Rocky Point	5,850	607,557	1.0	2	532
Top Sail	19,841	454,414	4.4	4	863
Union	26,109	843,428	3.1	5	580
Grady	2,965	173,903	1.1	3	297
Caswell	8,370	433,070	1.9	2	930
Columbia	6,233	481,175	1.3	2	445
Burgaw	63,547	1,326,694	4.8	6	895
Canetuck	11,505	232,148	5.0	35.0	131

The townships within the same county show even greater variations than are found between counties. For example, in different townships:

In McDowell County, the number listing varies from 0 to 11 per 100.

In Guilford County, the number listing varies from 4 to 21 per 100.

In Johnston County, the number listing varies from 4 to 30 per 100.

In Pender County, the number listing varies from 0 to 35 per 100.

In average amount listed per person listing:

In McDowell County, the amount varies from $323 to $2,157.

In Guilford County, the amount varies from $861 to $4,002.

In Johnston County, the amount varies from $246 to $4,703.

In Pender County, the amount varies from $130 to $1,172.

Here are two townships in the same county (Pender), in one of which every third person lists intangibles, while in the other only one person in the entire township so lists. In Johnston County the highest township produces seven and one-half times as many listings per 100 taxpayers as the lowest township. In amount per person listing, the highest township in Pender County (Holly) produces nine times as much as the lowest (Long Creek), while the highest in Johnston County (Pine Level) shows twenty times as much as the lowest (Boon Hill). All of these four townships last mentioned are rural. These extreme differences are certainly greater than the actual differences in ownership. Efficiency of the various tax listers is apparently revealed.

5. *How Much Revenue Are We Getting from Intangibles at Present?* As is generally known, our state government does not impose any tax on property. The revenue from intangibles, therefore, flows to the counties and towns. All intangibles pay a county tax, while those listed by town residents pay a town tax in addition. From the data gathered in 10 counties, it is possible to estimate the amount of intangibles listed by town people and country people respectively (see Table 7). These 10 counties show that about

61 per cent of the intangibles listed in those counties are listed by town people. Assuming that these counties are typical, then 61 per cent of the intangibles in the state pay a town tax in addition to the county tax. Furthermore, 75 per cent of property outside of towns lies in special charter school districts, according to data gathered by the Educational Commission. Taking all these factors into account, we get the following:

TABLE 14. ESTIMATED REVENUE FROM INTANGIBLES, 1927

$150,469,000 paying an average county-wide tax rate of $1.23 per $100,* yielded to the counties of the state	$1,850,769
Of the total amount of intangibles, 61 per cent ($91,786.00) paying an average town tax rate of $1.47 per $100,** yielded to the towns and cities	1,349,254
Of the intangibles outside of towns, 75 per cent lie in special school districts (75 per cent of $58,683,000 or $44,012,000) paying an average school district rate of $.40 per $100,*** yielded to the school districts outside of towns	176,048
Total revenue from intangibles	$3,376,071

*Rate obtained by dividing total county taxes for 1927 by total assessed value of property in counties in 1927.

**Rate obtained by method similar to the above, except 1926 figures had to be used.

***Rate obtained by similar methods, using figures compiled by State Educational Commission for the year 1926.

It appears from this analysis that intangibles provided about $3,400,000 of revenue to our local government in 1927. Since total local government revenues in that year amounted to approximately $62,000,000,[4] it is evident that intangibles contributed approximately 5.5 per cent of total local revenues.

Summary. The amount of intangibles on the tax books has steadily declined since 1921, in spite of the growth of wealth and population in the state. We are now listing less than $52 per capita, compared with almost $74 in 1921, and compared with $160 in Virginia and $353 in Kentucky.

Only about 2 per cent of our intangibles listed consists of bonds, almost 20 per cent is bank deposits, over 50 per cent notes and mortgages, and 25 per cent book accounts and claims.

In 16 counties of the state averaged together, only 9 per cent of those listing property listed intangibles. In 10 counties studied, one in 11 country taxpayers listed intangibles compared to one in 14 city taxpayers. The average listing of the city people was $2,310 compared with $1,357 for the country, the higher figure reflecting the listings of business firms in the cities.

In 12 fairly representative counties, corporations listed about 36 per cent of all solvent credits listed in those counties, though owning but 21.5 per cent of the real estate in the counties. A small sample of corporation tax abstracts shows that one in every 5 corporations lists solvent credits to an average amount of $13,495.

Between counties adjacent to one another, marked differences appear in both the amount of solvent credits listed and in the percentage that intangibles are of total property. Several counties show from three to five times as high a percentage as the adjoining county. There seems to be little relation between a county's tax rate and the amount of solvent credits listed. Between town-

[4]Based on the actual amount levied in the counties for 1927, and estimated amount levied in towns and special school districts based on 1926 levy.

ships within the same county the number of taxpayers listing intangibles varies from zero to 35 per 100, while the amount listed runs from $246 to $4,703 per person.

Our counties, towns, and school districts collected approximately $3,400,000 in revenue from intangibles in 1927. This was about five and one-half per cent of their total revenues.

II. Why is the Present Situation Unsatisfactory?

Having ascertained the facts, it is next in order to appraise the situation. Are we getting satisfactory results from the present method of taxing intangibles? If not, why not?

We must not be unduly critical of the tax on intangibles nor expect too much of it, for we are dealing here with a type of property that has always and everywhere baffled tax officials. Intangibles are easily concealed. They are easily moved from one place to another. It is difficult, and in some cases impossible, for assessors to get them on the tax books unless the owner is willing. Many forms of intangibles, such as bonds and mortgages, represent merely an interest in property already taxed. To tax the mortgage in addition to the real estate is double taxation, which seems to many persons unjust. Accordingly, we should judge the attempt to tax intangibles, not by standards of perfection, nor even by the standards we apply to such tangible property as real estate, but more leniently. It may be judged by its own past performance in this state, by its present performance in different counties of the state, and, to some extent, by comparing its experience here with the experience in other states. The chief criticisms that may be laid at the door of the intangibles property tax in this state are:

1. The amount of intangibles on the tax books is persistently declining.
2. Dishonesty and evasion are fostered, with relatively few persons bearing the tax.
3. Legal exemptions are developing an undesirable investment situation in the state.
4. Serious differences in the efficiency of administration are found among counties.

1. *The Amount of Intangibles on the Tax Book is Persistently Declining.* Table 1 shows the extent to which intangibles are moving off the tax books. The effect of this is to throw a heavier burden on other forms of property, especially real estate. The relative burden carried by each class of property may be seen in the following table:

TABLE 15. RELATIVE AMOUNTS OF DIFFERENT CLASSES OF PROPERTY ASSESSED IN 1921 AND 1927
(Data from reports of Commissioner of Revenue)

Kind of property	Amount assessed in thousands of dollars in		Percentage of total assessed in	
	1921	1927	1921	1927
Solvent credits	192,829	150,469	8.	5.
Real estate	1,625,094	2,041,366	63.	70.
Tangible personal	408,053	403,223	16.	14.
Public service companies, corporation excess and miscellaneous	353,797	324,558	13.	11
Total	2,579,773	2,919,616	100.	100.

During these six years it is doubtless true that all of these forms of property increased in value, yet real estate alone shows it on the tax books. Intangibles decreased more than any other item. It is evident, therefore, that other forms of property are now bearing relatively less of the tax burden and real estate is bearing relatively more than in 1921. Whether or not this is a desirable tendency is debatable, but, assuming that we want each form of property to continue to contribute in proportion to its past contribution, we are departing farther and farther from the goal.

2. *Dishonesty and Evasion Are Fostered, With Relatively Few Persons Bearing the Tax.* Taxing intangibles at the high rates imposed on other property encourages people to hide their intangibles, or place their money in exempt forms. The higher the tax rate, the greater the incentive becomes to evade the tax. The income return on most forms of intangibles is low. Bank deposits, commercial and savings, yield from 0 to 4 per cent. Safe bonds pay from 3½ to 6 per cent; promissory notes and mortgages are restricted by law in this state to not more than 6 per cent; conservative stocks yield about the same as bonds and mortgages. When the taxing authorities impose a rate of 2½ per cent on the principal it may mean the taking of 40 to 60 per cent of the income from the intangible property. The following table shows what percentage of the income from intangibles is taken by different tax rates.

TABLE 16. PERCENTAGE OF INCOME TAKEN BY VARIOUS TAX RATES ON INTANGIBLES

If the intangible yields an income of:	PER CENT					
	1	2	3	4	5	6
And the tax rate is 1 per cent, the percentage of income is:	100	50	33 1-3	25	20	16 2-3
A tax rate of 1½ per cent takes in percentage:	150	75	50	37 1-2	30	25
A tax rate of 2 per cent takes:	200	100	66 2-3	50	40	33 1-2
A tax rate of 2½ per cent takes:	250	125	83 1-3	62 1-2	50	41 2-3
A tax rate of 3 per cent takes:	300	150	100	75	60	50

Remembering that combined county and town tax rates average between 2½ and 3 per cent ($2.70 per $100 in 1927), it is clear that many owners of intangibles face virtual confiscation of their income, except as they may be able to shift the tax to some one else. Our high taxes, therefore, in so far as they are actually paid, come out of the income of the owner of the intangibles. Whereas we would not for a moment consider imposing an outright income tax of 50 per cent, we attempt to levy just such a tax indirectly.

Nor can the owner, as a rule, escape the blow by seeing his intangibles under-assessed, a practice commonly and openly employed with other property. Since the amount of principal is usually plainly stated on the face of the instrument, intangibles, when caught, ordinarily go down at full value. With assessment at 100 per cent of true value and confiscatory tax rates, it is little wonder that much of this property either hides or flees into exempt forms.

Our policy makes it profitable for people to be dishonest. The ease with which intangibles can be hidden makes it possible for them to be dishonest. When one man knows that his neighbor is not listing his intangibles he wonders why he should list his own. Thus a progressive deterioration is likely to ensue. Our tax laws ought to encourage honesty, but they actually do encourage dishonesty.

It should not be inferred that our particular system is responsible for all of the faults of intangible property taxation. Even if rates were low and assessments were made at a fraction of true value, there would be dishonesty and evasion, as other states can testify. But other things being equal, there will undoubtedly be more evasion under high rates than under low rates.[5]

In recent years our local tax rates have been steadily rising. County rates, shown in Table 17, probably represent fairly accurately the trend of all local rates.

TABLE 17. COUNTY TAXES, VALUATIONS, AND TAX RATES IN THE STATE, 1921-1927

(Data from reports of Commissioner of Revenue)

Fiscal year	County taxes on property	Assessed value of property in counties	Average county tax rate per $100
1921	$ 21,853,700	$ 2,579,772,023	$ .85
1922	22,533,185	2,576,338,426	.87
1923	27,626,451	2,657,141,169	1.04
1924	29,140,056	2,711,783,919	1.07
1925	31,746,117	2,746,915,916	1.16
1926	33,442,235	2,798,293,601	1.20
1927	36,105,822	2,934,011,733	1.23

According to this table, average county tax rates have increased in 7 years from 85 cents to $1.23, or 45 per cent. Table 2 shows that during the same period intangibles listed decreased 22 per cent. The former has unquestionably helped to produce the latter.

It would be unfair to leave the impression that the decline of intangibles on the tax books is due wholly to dishonesty and evasion. While it is doubtless true that many persons commit perjury when listing their property, it is also true that many persons carefully observe the law and still list no solvent credits. The legal avenues of escape for intangibles are discussed later.

Whether escaping honestly or dishonestly, those who escape outnumber those who pay ten to one. The table on page 51 shows that in several counties studied only two or three out of 100 paid a tax on intangible property. In one county the number rose to 23 out of 100, but the average for the 19 counties was only 9 out of every 100. It is probably fair to say that the tax is falling on the conscientious who do not try to escape, on the ignorant who do not know how to escape, on estates which cannot escape, and on certain corporations.

[5]It is true that Table 9 on page 54 shows little or no relation between rates and amount listed. But other factors, especially efficiency of assessment, are at work here. Then, too, the difference in rates are comparatively slight.

Incidentally, it may be pointed out that our system of taxing intangibles puts our state at a disadvantage in comparison with other states as a place of residence for the owner of intangibles. Some owners of intangible property are in a position to establish their legal residence in any one of several states. They will usually go to a state that deals leniently, or as they would say, fairly, with intangible property. It is not suggested that North Carolina should enter into competition with other states to attract wealthy residents by extending tax favors. We might, however, frame laws in line with the practice of other states, thereby aiming not to repel such persons.

3. *Legal Exemptions Are Developing an Undesirable Investment Situation in the State.* The methods by which our residents may lawfully escape the tax on intangibles are: (1) through indebtedness offsetting their intangibles; (2) through investments in tax-exempt bonds; and (3) through investments in shares of stock of domestic and foreign corporations.

The permission to deduct debts from intangibles owned doubtless increases the willingness of some persons to list their intangibles, knowing that they may offset their holdings, partially or wholly, by indebtedness. On the other hand, it opens the door to evasion through the creation of fictitious debts. So long as we tax intangibles at a high rate equity will demand that debts be deductible. If intangibles were segregated for taxation at a low rate, justice would not demand the deduction of debts.[6]

Investments in tax-exempt bonds are a matter which is very largely beyond the control of our taxing authorities. Bonds of the Federal Government and of the Federal and Joint Stock Land Banks are made non-taxable by Federal law. State of North Carolina bonds are exempted by state law with a view to promoting their marketability, as well as their issue at more favorable interest rates. County, municipal, and school district bonds are usually sold outside the state, hence raise no question of taxability in North Carolina. If they were sold within the state, they would presumably be taxable. It should be noted that tax-exempt bonds yield to the owner approximately as much income as 6 per cent taxable bonds would yield if the owner paid taxes on the latter at the average rate prevailing in the counties and towns at present.

The most serious avenue of escape for intangibles is the exemption of shares of stock. The exemption of shares in domestic corporations has some justification on the ground that the shares merely represent an investment in a corporation whose property has already been taxed somewhere, presumably in this state. But shares in foreign corporations can not make a similar claim. True, the property of foreign corporations has been taxed somewhere, presumably, and if we wish to avoid double taxation the shares should be exempt. But if we propose to exempt foreign stock in order to avoid double taxation, we should, to be consistent, also exempt corporation bonds, since they, too, merely represent an investment in corporate property already taxed. Consistency would demand further that all real estate mortgages be exempted on similar grounds. In fact, comparatively little intangible property would be

[6]Except, possibly, in the case of business firms whose current liabilities might properly be subtracted from cash, receivables, and securities owned.

left to tax if we started out to exempt all that represents an interest in property already taxed. Foreign stock exemption cannot be supported on the ground of avoiding double taxation without undermining all taxation of intangibles.

The exemption of shares of foreign corporations has at least two objectionable results. First, it opens the door to evasion through the creation of holding companies, and, second, it develops an undesirable investment situation in the state by encouraging investment in stocks to the detriment of other forms, such as bonds and mortgages. The first result is obvious. If a resident owns taxable intangibles and desires to escape property taxation on them, he may incorporate a holding company to hold the intangibles. He of course owns the stock of the holding company, tax free. If he is careful to choose as the home of his corporation a state having no tax on intangibles, such as Delaware, then neither he nor his corporation pays any tax on the property. He could not evade the tax by forming a domestic corporation, since North Carolina corporations are required to list and pay taxes on their net solvent credits.

The second result of stock exemption applies to a certain extent to domestic as well as to foreign shares. Our citizens are encouraged to invest their money in stocks rather than in bonds and mortgages. This means that the state, by its tax laws, is fostering the relatively riskier forms of investment. Not that all stocks are riskier than bonds or mortgages. But in general it holds true that bonds and mortgages, since they represent a loan of money, are better secured than shares of stock which represent a final and residual claim on the assets of a corporation. Some of our citizens are in a position to assume the risks of stock ownership. They should buy stocks. Others are not in a position to assume those risks. They should buy more conservative investments, but our tax laws are forbidding.

That our citizens are investing in stocks much more heavily than in bonds, notes, and mortgages is evidenced by the fact that the individual income tax returns to the Federal Government show that North Carolina individuals received $26,783,000 in dividends compared to $8,234,000 in interest and investment income in 1925. This is a considerably lower ratio than any of our neighboring states shows, as the following table reveals:

TABLE 18. PERCENTAGE RATIO OF INTEREST INCOME TO DIVIDENDS IN SELECTED STATES, 1925[7]

	Per cent
North Carolina	30.8
Virginia	46.5
Kentucky	38.1
Tennessee	46.7
South Carolina	84.1
Average for United States	52.3

While our tax laws are only one of a number of possible factors contributing to this result, they undoubtedly do so contribute. They place a premium on stock investments. It seems rather anomalous for a county official to say to a taxpayer, "If you put your money in Virginia county or city bonds you will be taxed, but if you put it in the stock of a Virginia corporation you will not be taxed!"

[7]Data taken from United States Treasury Department, *Statistics of Income for 1925*, p. 100.

A somewhat similar avenue of escape is provided by certain building and loan shares. Shares of these associations are commonly of two kinds: installment shares and paid-up shares. The latter are in reality simply money deposits which may be made at any time by any person. They are essentially identical with savings deposits made in banks. Yet the savings deposit in the bank, paying typically 4 per cent interest, is taxable, while that in a building and loan association, paying typically 5 per cent interest, is non-taxable.[8] Building and loan associations are worthy enterprises but it is doubtful whether the state is justified in giving them, through its taxation laws, such a competitive advantage over banks.

The same holds true of industrial and Morris Plan banks. It would seem to be better to tax money placed in these three institutions alike.

4. *Serious Differences in the Efficiency of Administration Are Found Among Counties.* Tables 9 and 10 suggest that all is not well with the administration of our law. One county shows four times as high a percentage of solvent credits to total property as an adjoining county. The highest county shows 10 times as high a percentage of taxpayers listing intangibles as does the lowest county in the group. Even greater differences are found among townships within the same county (see Table 11.) In view of these serious differences in listings, our system of administering the law is brought into question.

Our system is briefly as follows: the state authorities, in possession of certain information regarding intangibles through income tax returns, corporation reports, and otherwise, lend no assistance whatever to local officials. Listing is left entirely to the county officials. The county commissioners appoint a county supervisor of assessments, who may be and frequently is a person holding another county office, such as accountant or auditor (Machinery Act, 192, Sec. 43). This supervisor appoints an assistant for each township (Sec. 43). Before these assistants the citizens are asked to appear and list their property as of the first day of May (Secs. 44 and 54). It is the duty of this list-taker "to ascertain by visitation, investigation, or otherwise the actual cash value in money of each piece or class of property in his townships," and "to be constantly looking out for property which has not been listed for taxation" (Secs. 44 and 49). These duties become practically impossible of thorough performance, since listing begins on the first Tuesday after the first Monday in May and ends on the third Monday in June (Secs. 43 and 70). The county commissioners have the power to summon any taxpayer to answer as to the amount of his solvent credits and indebtedness (Sec. 64). Furthermore, it is the legal duty of the commissioners to employ a man to make a diligent search for unlisted property (Sec. 73).

These various provisions testify to a somewhat haphazard procedure which has developed in the course of time. The responsibility for assessments is

[8]Non-taxable, that is, to the holder of the paid-up shares. The association pays a tax of 12 cents per $100 share on all its shares. That the use of paid-up shares is increasing rapidly is shown by the fact that during the calendar year 1927 the amount of paid-up stock increased 17 per cent, while that of installment stock increased only 5 per cent. Paid-up stock, or its equivalent under other names, amounted to 24 million dollars on Dec. 31, 1927, compared to 56 million dollars of installment stock. (Figures from report of the associations filed with the insurance department of the state.)

not concentrated and clean-cut. The commissioners are theoretically responsible. They delegate the work to a supervisor, who undertakes it as a part-time job. So far as personal property is concerned, taxpayers practically assess themselves. The entire procedure is carried out, with rare exceptions, in the courthouse in six weeks' time or less. Then the assessment machinery is practically dissolved for a year. The system fails to keep a trained person on the job continuously. It fails to check up on unlisted property. It fails to transplant the best methods developed in other states and counties into counties needing better methods. Most of these faults in our assessment machinery, by the way, apply not only to intangibles but also to the more important forms of property, tangible personal property, and real estate.

With a system lacking coördination and central supervision, the natural result is wide diversity in assessments. Some diversity in results would occur even under the best administrative conditions. But the diversity would certainly be less than now prevails if we had greater uniformity of practice. No one can travel from courthouse to courthouse, examining records and interviewing local tax officials, as the commission's investigators have been doing, without coming to the conclusion that the amount of personal property on the books could be enormously increased if the efficiency of all list-takers were brought up to somewhere near the level of the best 10 per cent.

Summary. The present situation is unsatisfactory because the amount of intangibles on the tax books is persistently declining when it ought to be increasing, thrusting a larger share of the tax burden on real estate. Dishonesty and evasion are fostered by our high tax rates, which prove confiscatory when applied to the average item of intangible property. Only about one person in eleven lists intangibles, showing that the tax is now falling on a relatively few. These few are not necessarily the wealthy but may only be the conscientious, the honest, the ignorant, and the estates whose records are public. Our tax system tends to put the state at a disadvantage in comparison with other states as a place of residence for the owner of intangibles.

Legal exemptions help to explain the present situation. Permission to deduct debts from one's holding of intangible property relieves many persons —some honestly, some dishonestly—through the creation of fictitious debts. Tax-exempt bonds become attractive when high tax rates reduce the yield on other securities. Most serious of all is the exemption of shares of stock, especially of foreign corporations. This permits the organization of holding companies to own taxable securities, the individual owning the shares of the holding company tax free. The exemption of shares of stock furthermore encourages our people to invest their money in stocks rather than in bonds and mortgages, thus tending to produce an unbalanced investment situation in the state.

The administration of the law is unsatisfactory, evidenced by the glaring contrasts between counties in their listings of intangibles. Allowing the taxpayer to assess himself on his intangibles, with little or no checking up on omitted and undervalued items, not only allows millions of property to escape but tends to bring all tax administration into disrepute with our citizens.

III. What May be Done

There are three possible courses of action that we might follow in dealing with the problem of intangible property taxation. They are:

1. Continue the present system of taxing intangibles under the general property tax.
2. Give complete exemption to intangible property.
3. Place intangibles in a separate class of property, applying a low rate to this class.

Several combinations of these methods are also feasible, by which some forms of intangibles might be exempt while other forms might be taxed, either as general property or as classified property at a low rate.

1. *We Might Continue the Present System of Taxing Intangibles Under the General Property Tax.* The present system is not entirely a failure. The fact that it produces over three million dollars in taxes annually marks it as a fair revenue producer.[9] It has the advantage of simplicity, all property being treated alike. It does not invite log-rolling and appeals of special interests to have their intangibles exempted or placed in an especially favored class.

If the present system is retained, careful attention should be given to improving its administration. The glaring discrepancies between neighboring counties and among townships within the same county should be lessened. Only intelligent and competent list-takers should be employed. They should be given careful instructions as to how to question taxpayers regarding their solvent credits. A list-taker who succeeds in getting a high percentage of solvent credits on the books might be given some kind of public recognition and his methods might be taken over by others. Every practicable check-up of intangibles should be made. When a man claims debts offsetting his credits he should be made to itemize the same in order to see whether those owing to persons in the county are listed for taxation. This is now required by law but often is not enforced. Mortgages recorded in the county should be checked against those listed for taxes. Banks might be required to report all collateral put up as security for loans. Estates settled in the county reveal intangibles which should be followed up. The State Department of Revenue obtains valuable information on intangibles through reports filed with it. This information might be made available to local assessing authorities.

The objections to maintaining the present system are serious. They have been discussed in Section II. As there shown, the tax is falling on a few and is falling with almost crushing severity on these few. More and more intangibles are sliding out from under the tax, a process made easy by our exemptions and weak administration. So long as many persons are escaping, there will be a widespread feeling, both among tax officials and taxpayers, that it is unfair to press the matter of listing vigorously. Our comparatively high rates

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[9]This figure may be compared with the amount yielded by low-rate taxes on intangibles in the following states in 1926 (Leland, *The Classified Property Tax in the United States*, p. 274):

Minnesota	$1,242,000
Virginia	1,572,000
Kentucky	2,622,000

of property tax also weaken the will of enforcing officials, since they realize the confiscatory nature of the tax.

2. *We Might Give Complete Exemption to Intangible Property.* Complete exemption of intangibles might be urged on several grounds. The first is administrative convenience. Since it is not possible to get anything like all intangibles on the tax books, and since it is unfair to the few who are caught that the many escape, simply to give up the attempt to tax such property is the argument. Another reason advanced for complete exemption is that intangibles are for the most part merely paper representatives of real property already taxed. To tax intangibles means, therefore, double taxation. Since double taxation of property is assumed to be undesirable, the conclusion seems to follow that intangibles should be exempt. A third argument for exemption is that through our state income tax we are obtaining a contribution to government from the owners of intangibles, hence we need not tax them further. The adoption of the state income tax has been accompanied by the exemption of intangibles from the property tax in New York, Massachusetts, New Hampshire, Delaware, Wisconsin, North Dakota, and Mississippi. In fact, the breakdown of the property tax on intangibles was a prime reason for the adoption of an income tax in several of these states. For this reason, perhaps, the income tax has often been considered an alternative to the property tax on intangibles. Of the twelve states which are at present using the personal income tax, the seven named above exempt intangibles, three (Missouri, Oklahoma, and Virginia) tax them as property at a low rate, while only North Carolina and South Carolina continue to treat intangibles as general property.

Opposed to complete exemption are several considerations. The loss of revenue would be appreciable and would have to be made up by increased taxes elsewhere, probably on other property. There is serious doubt, also, whether public opinion in the state would ratify such a proposal. There is still a widespread feeling that the owners of intangibles are able to pay taxes and should pay them.

3. *We Might Place Intangibles in a Separate Class of Property, Applying a Low Rate on Them.* The movement to classify property, with the application of a different rate on each class, has attained considerable proportions in the United States. An investigation of the classified property tax, completed in 1927, showed that thirty states and the District of Columbia had the constitutional right to classify property for taxation.[10] The majority of these states were using the power; a few using it to classify real property into such

[10]The states are:

Arizona	Iowa	Minnesota	Oklahoma
California	Kansas	Montana	Oregon
Colorado	Kentucky	Nebraska	Pennsylvania
Connecticut	Maine	New Jersey	Rhode Island
Delaware	Louisiana	New Mexico	South Dakota
Florida	Maryland	New York	Vermont
Idaho	Massachusetts	North Dakota	Virginia
	Michigan		

In addition, Alabama, through a liberal interpretation of her constitution by the state supreme court, is able to use one form of classification; namely, the mortgage registry tax. (Leland, *The Classified Property Tax*, pp. 88-96. Houghton Mifflin Co., 1928.)

classes as forest land, mineral land, and farming land; a few using it to classify tangible personal property, such as livestock and household goods; but most of them using it for intangible property. For intangibles its use varies all the way from a special tax on bank deposits only, or a mortgage recording tax only, to elaborate systems of classification, with a different rate on each class of intangibles.

The arguments usually advanced for classification of intangibles are that the low-rate taxation is both equitable and expedient when dealing with this class of property. It is equitable because this class of property yields, on the average, a low or moderate return and is usually assessed at 100 per cent of true value, when assessed at all. Justice demands, therefore, the imposition of a low rate so as not to prove confiscatory. The expediency argument stresses the difficulty, amounting almost to impossibility, of getting intangibles on the books when high rates are imposed. Low rates are much more likely to win the coöperation of the taxpayer, which is essential if large amounts of this property are to be placed on the books. A low rate invites a citizen to be honorable in listing his property. Then, too, it is argued that officials can zealously prosecute the search for intangibles if the rate is low and the tax is considered fair and just.

If low-rate taxation is to prove successful, it should produce one or both of two results, namely:

1. The amount of intangible property listed should be greatly increased, thereby broadening the base of the tax and distributing the burden more widely.
2. The yield in revenue should be as large as, or larger than, intangibles have been giving under the general property tax.

Judging by the experience of other states changing to low-rate taxation, we might well expect to obtain the first result but might not obtain the second.[11] Much depends upon the efficiency of administration, both state and local, and whether or not certain intangibles are taxed at the source.

A large part of the success or failure of classification can be laid at the door of administration. It will generally be found that states that are succeeding with the tax are states that have efficient administrators, especially in the state tax commission. States that have failed with the tax, or have made merely an indifferent showing, can usually trace the trouble to poor administration rather than to the law itself. No law, least of all a tax law, will operate itself. This is especially true in dealing with evasive property like intangibles. Successful administration of a classified property tax on intangibles requires the active coöperation of state and local authorities. The state authorities must work on certain phases of the task of enforcement for which their information and authority equip them. Local officials, dealing with the individual property owner, must persistently search for and check up intangibles. Between state and local officials there must be exchange of

[11]The experience of states using classification is carefully set forth in K. M. Williamson's *The Present Status of Low Rate Taxation of Intangible Property* (National Tax Association, 1925) and S. E. Leland's *The Classified Property Tax* (Houghton Mifflin Co., 1928).

information, development of high standards of procedure, and the transplanting of successful methods into areas where they are lacking. Unless we are reasonably sure of obtaining efficient administration, including thoroughgoing coöperation of state and local officials, we may as well keep the system we now have.

A second prerequisite to success is the collection of the tax at the source wherever practicable. It is especially practicable with bank deposits (taxed against the bank), with mortgages (taxed once and for all at the time of recording), and with certain shares of stock, such as building and loan associations and other financial institutions. Collection at the source avoids the necessity of going after the individual owner and persuading or forcing him to list his property. Moreover, it gets practically 100 per cent of the property liable for the tax, and at an expense which is usually lower than the other method.

If classification and low-rate taxation were adopted, the permission to deduct debts from solvent credits might well be withdrawn, except perhaps in the case of business enterprises. There is little or no injustice in asking the individual who owns securities as private investments to pay a light tax on his holdings without deducting his indebtedness. Such a policy would increase the listings of taxable intangibles, would simplify the task of listing, and eliminate the temptation to create fictitious debts. With business enterprises the case is somewhat different. A merchant may be doing a credit business, buying his merchandise on time and carrying customers on charge accounts. On May 1 he might have $200,000 of accounts receivable representing goods sold, but he might owe $150,000 for goods bought. Remembering that his goods on hand are taxable at full property tax rates, it may be unjust to tax him on the $200,000 of accounts receivable with no allowance for what he still owes on the goods. Similarly a company dealing in mortgages and other real estate paper might have a large amount of mortgage paper on hand but have borrowed heavily from banks and elsewhere to buy the paper. Ability to pay would be better represented by the excess of credits over debts than by the credits alone.

If classification were adopted, it might prove desirable to give the various types of intangibles different treatment. The main types to be considered are:

1. Bank deposits
2. Mortgages
3. Shares of stock
4. Bonds and notes
5. Accounts receivable

1. *Bank Deposits.* Judging by the bank deposits listed in 20 counties, summarized in Table 5, we had approximately $28,000,000 of deposits listed in the entire state in 1927, which is about eight per cent of the total bank deposits of that year. While we would unquestionably get a considerable increase in listings if we were to lower our rate of tax and still rely on the voluntary declaration of the taxpayer, that is not the most efficient way to tax bank deposits. To make all deposits pay and to make them pay at a

minimum of expense and trouble they should be taxed at the source, that is, against the bank.[12] Since the tax would be in lieu of a property tax on the depositor, the bank should be authorized to charge the tax against the depositor's account. If the rate were quite low, say 10 cents on the $100 (Kentucky's rate), the tax would not be burdensome on the depositor. Some banks might prefer to absorb the tax themselves rather than to compute and debit the tax to each account. The banks would be spared the trouble now caused them by certain depositors who withdraw their savings just before May 1 only to return them a few days later.

Since building and loan associations handle what amount to savings accounts in the form of their paid-up shares, these shares should be taxed like bank deposits. The same is true of the investment certificates of industrial and Morris Plan banks. If no deduction had been permitted from the amounts on the books of these institutions in 1927, the yield of such a tax would have been as follows:

TABLE 19. ESTIMATED YIELD OF A TAX OF 10 CENTS PER $100 LEVIED AT THE SOURCE ON MONEY ON DEPOSIT

(Data from reports of Comptroller of the Currency and insurance commissioner of the state)

Type of deposit	Amount in 1927	Yield of tax of 10 cents per $100
Deposits in banks	$ 200,696,000	$ 200,696
Savings deposits in banks	156,071,000	156,071
Paid-up shares in building and loan associations	24,127,000	24,127
Investment certificates in industrial banks	4,624,000	4,624
Total	$ 385,518,000	$ 385,518

Under the present system bank deposits yield approximately $63,000 a year in revenue. (Since they comprise 18.7 per cent of all intangibles listed, according to Table 5, they are estimated to yield 18.7 per cent of all the revenue from intangible property). The yield under the proposed system would be approximately $385,000, or over six times the present amount.[13]

2. *Mortgages.* Exemption from taxation is granted to mortgages in some states on the ground that the real estate behind the mortgage has been fully taxed and that to avoid double taxation the mortgage should be exempt. Some states make the exemption dependent upon the real estate being situated in the state granting the exemption.

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[12]The experience of Virginia and Kentucky is illuminating in this respect. In 1926, Virginia with a low rate on bank deposits but depending on individual assessments, listed only 20 per cent of her bank deposits (425 millions of deposits according to the Comptroller of the Currency's Report, with 86 millions of deposits listed for taxation, according to Governor Byrd's address before the general assembly, January 11, 1926.) In the same year Kentucky, with a low rate but assessing the tax against the bank, had 83 per cent of her deposits listed, most of the balance being exempt (335 millions assessed out of 404 millions of deposits, according to 1926 report of Kentucky Tax Commission, p. 99).

[13]In 1926 the following states taxed bank deposits at the source, the majority taxing savings deposits only: Connecticut, Kentucky, Maine, Massachusetts, Maryland, New Hampshire, New Jersey, Rhode Island, and Vermont. (Leland, *The Classified Property Tax*, p. 217; Williamson, "Bank Deposits Taxes in New England", *American Economic Review*, March, 1928, p. 45ff.)

If mortgages are to be taxed at all they should be by means of a registration tax, levied once and for all at the time the mortgage is recorded. This is applying the principle of taxation at the source and has the advantages of such taxation. Evasion is rare, especially if an adequate penalty is imposed for failure to register the mortgage. Ordinarily no penalty is needed, for the mortgagee desires to protect his lien by placing it on the county records. Computation and collection of the tax are easily administered through the register of deeds or clerk of court in the county. One of the chief advantages for a state like North Carolina is that outside capital coming into the state for investment in mortgages would pay the same tax that local capital pays. Under the present system this outside capital pays no tax whatever in this state, although it is being protected by the state.

It may be objected that the outside investor would not pay the tax, but would shift it to the borrower. If the tax were heavy and if alternative investments were available, equally attractive and tax-free, the tax would probably be shifted. However, if the tax were light and other available investments were also taxed, shifting probably would not occur. Only time and experience with the tax could give a final answer to this question.

If a registration tax were adopted, short-term mortgages should not be discriminated against by being charged the same tax as long-term mortgages. The Minnesota plan of one rate for short-term and a higher rate for long-term mortgages is preferable to the single rate plan.[14]

Mortgages outstanding at the time the new tax goes into effect should be relieved of the property tax thenceforward by paying the registration tax. This would increase considerably the revenue the first year as compared with that of subsequent years.

The registration tax might, of course, be broadened to apply to mortgages on personal property, and even to leases, deeds, and contracts registered in the county. To apply such a tax it would be necessary to require the true consideration to be shown on the document.

There are no figures available on which to base an estimate of the yield of such a tax. The experience of other states changing from an annual ad valorem tax to a registration tax indicates that the yield of the registration tax is generally somewhat higher but more variable from year to year than the property tax.[15] Much depends, of course, on the rates of the two taxes and on the activity of the real estate market.

It is possible that, even without a constitutional amendment permitting the classification of intangible property, North Carolina could adopt a registration

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[14]Minnesota charges 15 cents per $100 of debt secured by mortgage if the mortgage runs less than 5 years and 6 months; 25 cents per $100 if it runs longer than 5 years, 6 months. Other states use the following rates:

Alabama .....15 cents on each $100
Kansas .....25 cents on each $100
Kentucky .....20 cents on each $100
Michigan .....50 cents on each $100
Oklahoma..... 2 to 10 cents on each $100 depending on term of years the mortgage runs.
New York.....50 cents on each $100
Tennessee.....10 cents on each $100
Small mortgages exempt.
Virginia.....10 cents on each $100
Applies also to deeds, leases, and contracts recorded in the county.

[15]A brief analysis of the experience of states using the registration tax is found in Leland, *The Classified Property Tax*, pp. 195-203.

tax on mortgages as a privilege tax in lieu of all other taxes. This has been done in two states whose constitutions are similar to our own (Alabama and Tennessee) and their courts have upheld the tax.

3. *Shares of Stock.* Shares of stock of domestic corporations are now exempt from taxation on the ground that the real and personal property of the corporation has paid its tax, presumably within the state, and that to tax the shares separately would be objectionable double taxation; also on the ground that in so far as the corporation has high earning power with little or no tangible property we are reaching it through our corporate excess tax.[16]

Shares of foreign corporations, as pointed out on page 63, are entirely exempt. If the corporation owns property in this state, it pays on its tangible property but nothing on its corporate excess. If it owns no property in the state, neither it nor the resident shareholder pays anything. It is not the exemption of foreign stock *per se* that is objectionable but the discrimination involved in exempting stock and taxing bonds and other intangibles. All foreign securities should be treated alike—either all taxed or all exempted.

If shares of stock are made taxable, instead of exempting domestic and taxing foreign shares, a different distinction might well be made. All shares could be exempted to the extent that the property of the corporation is taxed within the state. Conversely, all shares owned by residents could be taxed to the extent that the corporation is not paying within the state on its property. This would mean that if a domestic corporation owned half of its property within the state and half outside, its shares owned by North Carolinians would be exempt only to 50 per cent of their value. If a foreign corporation had 25 per cent of its property in this state, 25 per cent of the value of its shares would be exempt on the part of the owner.

There is no reliable method by which to estimate the revenue obtainable from a low-rate tax on stock, levied on the basis suggested above. The Federal income tax returns for 1925 show $26,783,000 dividends received by North Carolina individuals filing returns. In addition, some dividends were received by persons not filing a return to the Federal Government. Capitalizing these dividends at a rate of 6 per cent gives a value of $446,383,000 to these shares. But what proportion of the value of these shares is represented by corporate property taxed in the state is not known. Neither is it known how much stock is owned by North Carolinians not represented in the dividends reported to the Federal Government. All that can be said is that, since we receive no revenue whatever from shares of stock in the hands of individuals at present, such as we might get from a low-rate tax would be clear gain as compared with the present system.[17]

4. *Bonds and Notes.* Of all intangibles, bonds and notes are the most difficult to assess. Whereas shares of stock, especially in domestic corporations, may be reached through the corporation, bank deposits through the bank,

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[16]The corporate excess is the amount by which the value of the capital stock exceeds the value of the real and personal property listed for taxation. In this state only domestic corporations are taxed on this excess. It is taxed as property by the local governments, along with the real and personal property of the corporations.

[17]In 1922, the last year in which we taxed stock in foreign corporations, the amount listed in the state was $22,650,414. (Report of Commissioner of Revenue, 1923, p. 15.)

accounts receivable through the balance sheets of business firms, and mortgagees through the recorder's office, bonds and notes defy detection at the source. In so far as they are owned by trustees or business firms which file reports with public officials, they may be checked. But in so far as they are held as private investments, their assessment depends almost entirely on the willingness of the owner to list them. Here is where low-rate taxation may help. It is easily possible that a low-rate tax on bonds and notes may not only bring on the books a much larger amount of these holdings, thereby spreading the burden of taxation more widely, but also that it may actually produce more revenue than a high rate.

Another advantage of low-rate taxation would be that our state would become a better market for bonds, thus tending to correct the unbalanced investment situation described on page 63. Some of our larger corporations offer to pay, for their bond-holders, the low-rate tax levied on their bonds by the various states. If North Carolina were included in such offers, we would obtain the revenue without involving any sacrifice of income on the part of our citizens.

5. *Accounts Receivable.* The table on page 50 indicates that about 25 per cent of our intangibles listed at present are book accounts, including miscellaneous claims against debtors. It is probable that most of these are listed by business enterprises. At present no attempt is made to check these listings against the reports filed with the state for income and franchise tax purposes. Under classification and reduced rates, all possible sources of checking should be used in order to prevent a falling off in revenue from this source.

Summary. There are three courses of action open to the state. We might continue the present system, we might give complete exemption to intangibles, or we might classify intangible property, applying a different rate from that on other property. Combinations of certain elements in the three plans are also feasible.

In favor of retaining the present system, the principal arguments are that it yields a fair amount of revenue and that by treating all property alike we avoid the bickerings of special interests to have their property exempted or favored by low rates. The chief objections to the present system are that the tax is falling on a few, that rising tax rates make the burden quite serious for these few, that more and more intangibles are escaping the tax, honestly and dishonestly, and that weak administration of the law is traceable partly to the high rates imposed. If the present system is retained, every effort should be made to plug up the leaks and strengthen enforcement.

Complete exemption may be urged on the grounds that it is impossible to administer a tax on intangible property with anything like the efficiency that a tax on tangible property can be administered, hence the attempt should not be made; that most intangibles are merely paper representatives of real property already taxed, and therefore taxation of the intangibles represents double taxation; that the adoption of the state income tax has been accompanied by the exemption of intangibles in the majority of states using the

personal income tax, and that the income tax should be considered as a substitute for a property tax on intangibles. Opposed to exemption are the loss of revenue involved and the widespread feeling that owners of intangibles are quite able to pay taxes and should pay them.

Classification of intangible property with a different rate on such property is permitted by the constitutions of some thirty states, the majority of which are using the power. Arguments for the step are that we would be getting into line with the general trend throughout the country; that it is equitable to tax intangibles at a lower rate than other property in view of the lower average income return on such property and the higher percentage of true value at which it is assessed; that it is expedient to impose a lower rate in view of the ease with which this property may be concealed and in view of the necessity of gaining the coöperation of the taxpayer; and that a low-rate encourages officials to a more zealous enforcement than a high rate. If classification is to be considered successful, it should greatly increase the amount of intangibles on the tax books, thus distributing the burden more widely; in addition, it should yield close to or quite as much revenue as the present system. Whether or not we could expect such results would depend mainly on the kind of administration we secured and how the law was drafted. If collection at the source were used wherever practicable and if debts were not deductible, the results, assuming reasonably good administration, would probably justify the change.

Bank deposits can most effectively be taxed at the source, i.e., against the bank, with authority to charge the tax to the depositor's account. Mortgages, likewise, can be reached at the source by a recording tax levied once and for all at the time the mortgage is recorded. Shares of stock, both foreign and domestic, might well be taxed to the extent that the property of the corporation has not been taxed within the state. Bonds, notes, and accounts must be reached largely through the voluntary listing of the owner, a process that may be stimulated by a low rate.

INTERSTATE COMPARISON OF THE TAX BURDEN ON COTTON MILLS

(Limited to State and Local Taxes)

Hershal L. Macon, *Randolph County, N. C.*

Complaints registered by manufacturers against high taxes are entirely normal. Not only manufacturers but other business men, and farmers as well, periodically appear before the legislature with the claim that they are being taxed excessively, or are being required to pay more than their proportionate amount of the revenues raised. In many instances these contentions are nothing more than idle talk no doubt, while in others there is a measure of truth.

From recent articles carried in the various trade and commercial journals it might be concluded that the high taxes in the New England states and the low taxes in the South are important factors in the movement of the textile industry to the southern states. The tax system of Virginia has been revised during the last three or four years and made much more attractive to capital. According to a recent article in the *N. Y. Journal of Commerce,* there is now over $40,000,000 invested in the rayon industry in Virginia, with an annual output of about $30,000,000 and a payroll of $10,000,000. A part of this and other expansions may be the result of reduced taxes, or other factors may account for it.

Governor Fuller, of Massachusetts, in his inaugural address before the legislature[1] discussed the tax question and warned against going beyond the point of safety in taxing industry. To quote from this paper: "It is an open question whether we have not traveled so far in the protection we give labor and in the advantages—both state and municipal—that we give our citizens in good roads, education and other facilities, that, between the expenditures we have imposed on industry and the taxes that we and the cities and towns exact from them, our industries have not reached a position where there is nothing left for a good many of them to do but to quit."

This leads to the question—just what is the truth about the taxes and how much is mere talk? If taxation is a very important factor in the movement of industry South, it is strange that there is not more said about the discrimination in rates within the state. While it is usually agreed that taxes are of minor importance, nevertheless, if an industry is on the decline, or is operating on a very low margin of profit, taxes may be a determining factor.

In attempting a comparison of the taxes levied the first big effort is that of measuring the tax burden. If this can be done, then it is possible to compare the taxes on various industries and between the different states. There is no scientific way worked out for making this comparison. The popular idea is that the ratio of taxes to income shows the burden. That certainly measures the amount of the taxes but it does not go far enough. In the first place it assumes that all taxes are borne and not shifted. Taxes may be advanced by one individual or business while the real burden is shifted elsewhere to the

[1] *N. Y. Journal of Commerce.*

consumer. A simple illustration of this is the gasoline dealer or the theatre manager. In either of these cases the money is advanced, but the burden is passed on to the consumer.

To say that the real burden is the amount of taxes not shifted does not allow for the fact that some taxes are for special benefits. An illustration here would be the paving of streets, or the installation of a lighting system, fire protection, water and sewer systems. Cotton mill owners often provide these for their mill villages rather than have taxes levied for that purpose. It is the same situation as going into the market and buying services or commodities. The idea that the ratio of taxes to income measures the tax burden is subject to these two qualifications at least.

To measure the tax burden accurately it is necessary to know the final incidence. For example, the general property tax on machinery will probably be shifted if all manufacturers have it to pay. If, however, the tax is paid in North Carolina and not in Virginia and the mill owners sell in the same competitive market, the tax would not be shifted. There is a tendency for the real property tax to be capitalized so that the new buyer is partially free from the tax burden.

Where investigations are made covering a large number and variety of industries it is found that the ratio of taxes to income varies widely. Industries which have a high fixed investment in real estate and other property pay a much higher ratio of taxes to income than an individual or business which has a small fixed investment in real estate. This comparison might be applied to a cotton mill on one hand and a broker, a banker, or a real estate business on the other, but it does not follow that because the former pays a higher ratio of taxes that the tax burden is greater on the cotton industry. The rate of returns, allowing for risks, must be approaching equality, or else capital would not go into the cotton mill business but where the returns were greater. If the taxes were suddenly changed time would be required for readjustment, but, to the extent that the returns are equalized regardless of the ratio of taxes to income, the property tax is shifted and consequently is not a burden. This would be true within the state, or in an area with the same taxes, but in competition with cotton mill operators outside of the state it might not be shifted unless economic advantages in North Carolina were great enough to counterbalance the taxes. In case of public utilities, where a fair rate of return and no more is guaranteed, a tax on property would be shifted.

The other important tax to consider is the one on income. According to a report submitted by the Industrial Conference Board to the Joint Congressional Committee on Internal Revenue Taxation, the Federal corporate income tax is not shifted. Quoting from *The N. Y. Journal of Commerce,* March 19, 1928: "Federal corporation income tax can not be shifted onto the consumer; it does not affect prices, or the movement of capital investment excepting under unusual circumstances." If the Federal income tax, which is general is not shifted, then certainly a state income tax on industry would not be

shifted if the products of that industry were marketed in competition with goods produced where there was no income tax. From these general observations the assumption is that in a competitive industry—and the cotton textile business certainly comes in that group—the total taxes levied furnish a real basis for comparing the tax burden.

There are two methods which offer possibilities for comparing the amount of taxes levied. The first method suggesting itself is the study of facts concerning particular mills. This has the advantage of giving the actual taxes paid, the income, the size of the mill, extent of operations, the age of the plant and equipment, the type of machinery and products; also whether it is a spinning, weaving, finishing or specialty mill. To make this method effective would require the collection of a huge mass of data. Even in North Carolina there are 338 mills, according to the report of the Commissioner of Revenue for 1926. It would be possible to obtain information concerning 100 of these mills and still have very distorted ideas as to the average tax burden on the industry. If the profits are large the operators are indisposed to make it known, as it might be a fertile field for labor agitation, and furthermore, the profits of one good year are often depended on to tide the company over one or more years of low profits. The tax per spindle would serve very well in a limited number of instances, or rather for a particular type of mill. But even here there is a wide difference in the hours of operation and the quality of the product.

There is certainly an important advantage in having actual figures, and there is no attempt here to disparage this procedure. If the time and facilities were available and the information collected, any application to a particular mill would require adjustments which would be tedious and tiresome. The mill under consideration would not be identical with any other mill within the state and the differences would multiply as plants in other states were compared. It might be said with justification that the more exact the information is for a particular mill the more unreal for the whole.

The method used, which requires much less work, is that of calculating the taxes which a representative mill would pay in each of the particular locations selected. This representative mill is open to the criticism of being unreal and imaginary. It has the advantages of being the same in each location; it is free from extremes in size and age, and has a moderate rate of profits. While it does not give actual conditions, it does furnish a good basis from which adjustments can be made to meet specific instances. To make this method effective it is necessary to have a financial statement which is typical so far as possible. The figures used and the source are given on page 81. The net income, for which there would necessarily be adjustments where an income tax is levied, is given before any taxes are paid. Consequently the net income for calculating income taxes will vary inversely with the amount of other taxes paid.

The number of locations for which taxes were computed is small but it does include many of the leading textile centers. In making the selections cities and towns which would be comparable in size to those in North Caro-

lina were taken. There are exceptions, due to the difficulty in securing local rates and the fact that some of the cities of larger size are included—such as Fall River and New Bedford, Massachusetts—because they are widely known cotton manufacturing centers. Ten states, including North Carolina, are represented. While not covering the entire textile region, those states most frequently spoken of as our competitors are on the list. The states studied are: Massachusetts, Connecticut, New Jersey, Pennsylvania, Virginia, North Carolina, Tennessee, South Carolina, Georgia, and Alabama.

With the financial statement in readiness and the locations determined, the next step was to calculate the taxes which the hypothetical mill would pay in each place. To do this it was necessary to have both the local and state tax laws and levies.

The greater part of the information necessary for determining the state taxes came from bulletins and reports issued by the state tax commissions and departments of revenue. Special compilations of state tax laws, where they were available, proved very helpful. The local levies and the ratio of assessed to true valuation required for determining the general property tax, which is the largest tax in amount, were very difficult to secure.

To obtain this information about seventy letters were mailed to county and city tax supervisors. Thirty-nine replies, most of which were signed by some tax official, supplied the figures which are used in this study. The rates are all for 1927, with the exception of Massachusetts, where those for 1926 were the last ones available, and in four cities outside of Massachusetts for which the 1928 rates were supplied. The assessment ratios are only estimates, as no percentage can be more than an approximation. In all cases the ratios were given in a very general way and attention was often called to the customary variations.

Estimated Amount of State and Local Taxes Payable by Corporations with Specified Assets Under the Laws of the Various States

The following tables are intended to show the amount of state and local taxes levied on a hypothetical cotton mill in selected towns and cities in different states. Its purpose is to compare the tax burdens on textile manufacturing in various sections of North Carolina with those levied by other competing states. In the calculations it is assumed that the laws are uniformly enforced, although adjustments have been made to allow for the ratio the assessments bear to true value. The greater part of the data on local rates and assessments was taken from replies to letters mailed to city and county tax supervisors. The ratio of assessed to true value has been used as it was obtained from these sources without further investigation; at best such figures can be nothing more than estimates of the average.

The financial statement used was supplied by an accountant who considered it fairly representative of the average North Carolina mill. No attempt was made, however, to verify the statement either in regard to size or financial condition of the mills. The items of this balance sheet, which serve as a basis for all of the calculations, are shown on page 81. The findings

based on such an imaginary corporation cannot be considered as corresponding to actual conditions, due to the numerous peculiarities which are important to the individual mill.

It will be noted that Pennsylvania takes the first place on the list with the lowest taxes; Massachusetts has the last place with the highest taxes; while North Carolina comes seventh among the ten states compared. There is such a wide variation in the local tax rate that there can be little assurance that the locations selected are typical for the state being considered; however, it is believed that the results are representative of conditions as they exist.

COMPARISON OF STATE AND LOCAL TAXES, INCLUDING LOCAL RATES AND ASSESSMENTS, BASED ON THE BALANCE SHEET AS SHOWN FOR HYPOTHETICAL COTTON MILL—SCHEDULE 1

Location	Local rates	Assessment per cent	Adjusted rates	Local taxes	State taxes	Total taxes
Pennsylvania						
Allentown	$2.94	50	$1.47	$ 3,454.50	$	$ 3,454.50
Reading	2.70	50	1.35	3,172.50		3,172.50
Virginia						
Danville	1.75	52½	.918	4,814.25	2,273.11	7,087.36
Dan River D.*	2.20	27	.6116	3,204.78	2,158.48	5,363.26
Chesterfield Co.						
Manchester D.**	1.45	60	.87	3,340.80	2,330.25	5,671.05
Bermuda Dist.	1.90	60	1.14	5,973.60	2,287.80	8,261.40
Motoaca Dist.	2.00	60	1.20	6,288.00	2,278.37	8,566.37
Alabama						
Montgomery	2.60	30	.78	4,508.40	1,427.10	5,935.50
Linden	1.95	60	1.17	6,762.60	2,554.20	9,316.80
Birmingham	2.95	36	1.062	6,138.36	1,652.52	7,790.88
Connecticut						
New Britain	2.55	80	2.04	11,505.60	1,069.88	12,575.48
Meriden	2.70	65	1.755	9,898.20	1,102.03	11,000.23
Hartford	2.188	80	1.75	9,872.25	1,102.55	10,974.80
Middletown						
District 1**	3.00	80**	2.40	10,051.50	1,098.97	11,150.47
District 2	1.90	80**	1.52	6,365.95	1,172.68	7,538.63
Georgia						
Athens	3.30	50	1.65	9,966.00	1,710.00	11,676.00
Clarke Co.*	1.80	50	.90	5,436.00	1,710.00	7,146.00
Columbus	2.60	55**	1.32	7,972.80	1,445.75	9,418.55
Augusta	4.10	66 2-3**	2.38	14,427.55	1,770.40	16,197.95
New Jersey						
Passaic	2.896	62½	1.81	10,211.22	1,562.28	11,773.50
Plainfield	3.36	60	2.01	11,336.40	1,556.64	12,893.04
North Carolina						
Asheboro	2.85	65	1.85	11,189.10	2,993.31	14,182.41
Belmont	1.55	75	1.16	7,021.50	3,185.85	10,207.35
Bessemer City	2.00	75	1.50	9,060.00	3,094.12	12,154.12
Mount Holly	2.00	75	1.50	9,060.00	3,094.12	12,154.12
Burlington	3.65	60	2.19	13,227.60	2,906.58	16,134.18
Charlotte	2.38	68	1.62	9,775.14	3,061.94	12,837.08
Cherryville	2.10	75	1.57	9,513.00	3,073.73	12,586.73
Durham	2.50	60	1.50	9,060.00	3,094.12	12,154.12
Gastonia	2.40	75	1.80	10,472.00	3,025.58	13,497.58
Greensboro	2.09	75	1.57	9,467.70	3,075.77	12,545.47
Winston-Salem	1.55	68	1.05	6,366.16	3,215.34	9,581.50
Tennessee						
Chattanooga	2.86	65	1.859	10,745.02	1,553.95	12,298.97
Knoxville	2.80	90	2.52	14,565.60	1,781.31	16,346.91
South Carolina						
Greenville	5.725	10-38**		9,389.00	4,001.00	13,390.00
Charleston	9.775	42.6	4.16	25,151.46	3,850.75	29,002.21
Massachusetts						
Fall River	2.84	100	2.84	14,626.00	1,693.22	16,319.22
Lawrence	2.96	100	2.96	15,244.00	1,677.77	16,921.77
Lowell	3.34	100	3.34	17,201.00	1,628.85	18,829.85
New Bedford	2.78	80	2.224	11,493.60	1,771.53	13,265.13

*These are the rates for the county—outside of Danville and Athens.
**Assessments vary for different kinds of property.

SCHEDULE 1

COTTON MILL COMPANY*
BALANCE SHEET
December 31, 1927

ASSETS		
Cash		$ 26,000
Acceptance Receivable		7,000
Accounts Receivable		44,000
Inventories		
Cotton	$ 5,000	
Stock in Process	9,000	
Finished Goods	17,000	
Fuel and Supplies	9,000	40,000
Total Current Assets		$117,000
Plant and Equipment at Cost		
Land	$ 15,000	
Buildings	176,000	
Machinery and Equipment	481,000	
Tenements	83,000	
Other Equipment	9,000	
	764,000	
Less Dep. Reserve	240,000	524,000
Deferred Charges		1,000
Total Assets		$642,000
LIABILITIES		
Notes Payable		$ 35,000
Vouchers Payable		2,000
Accrued Wages		1,000
Total Current Liabilities		38,000
NET WORTH		
Capital Stock (Common)	$500,000	
Surplus	104,000	
Total Net Worth		$604,000
Total Liabilities and Net Worth		$642,000

TAX LAWS AND ORDINANCES

Pennsylvania

There is no state tax on manufacturing concerns except an organization tax and a 4-mill tax on bonds outstanding. There is a 5-mill tax on the actual value of capital stock, but this tax does not apply to capital "invested in and actually and exclusively employed in carrying on laundrying or manufacturing within the state." There is also an 8-mill tax on the gross receipts of public utilities.[1]

*The original balance sheet from which the above statement was taken was furnished by Mr. Karl E. Thies, C. P. A., of the Courter, Rhyne, Moore & Co., Textile Cost Accountants, of Charlotte and New York. Mr. Thies gave what he considered "a fairly representative balance sheet of a North Carolina cotton mill." The net profits for the year ending December 31, 1927, were given as $56,742.30 before Federal or state income taxes were paid. The net income as used in the calculations was increased to $65,000 in order to include the amount paid out for local taxes and other state taxes. The amount added was $8,257.70, which is near the average amount of local taxes paid in North Carolina.

[1]Laws relating to state taxation and revenue, 1926.

Virginia

State taxes:

Income tax, 3 per cent on entire net income[1]

Annual registration fee[2]

$25.00 when capital stock exceeds $300,000

Annual state franchise tax[3]

$100.00 when capital stock from $300,000 to $500,000

$200.00 when capital stock from $500,000 to $1,000,000

State property tax[4]

85c tax on capital

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[1]*Virginia Tax Laws*, 1926.
[2]*Ibid.* p. 64ff.
[3]*Ibid.* p. 133.
[4]*Ibid.* pp. 47-48.

Capital includes: (1) inventories, (2) excess of bills and accounts receivable, (3) moneys and deposits, (4) claims, equities, choses in action and other property. Capital is not taxed locally.

Alabama

State taxes:

Franchise tax[1]

60c per $1,000 of paid-up capital stock

Property tax[2]

65c on $100 valuation

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[1]*Report of New York State Tax Commission*, 1926.
Digest of State Laws Relating to Taxation and Revenue, 1922.
[2]President of Montgomery County Board of Education, Nov., 1927.

C. E. Rightor, of Detroit Bureau of Governmental Research. *National Municipal Review*, December, 1927.

Connecticut

State taxes:

Income tax[1]

2 per cent on net income

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[1]Statutes pertaining to the assessment and collection of property and personal taxes, State of Connecticut, 1926. The net income is the same as used by the United States Government.

This income tax is levied "in lieu of all taxes which otherwise would be laid on moneys and credits, including accounts and bills receivable, and shall be in lieu of all other taxes upon the franchise except tax on increased capital stock." This quotation comes from the Corporation Net Income Tax Law, 1921.

Georgia

State taxes:

Annual license tax[1]

Measure of the tax is capital stock

Rate: $300,000 to $500,000 capital, $200.00

Property tax[2]

5 mills; tax calculated for each separate location

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[1]Instructions of Comptroller General to Tax Receivers in Georgia, 1928-1929.
[2]R. C. Norman, State Tax Commissioner, March, 1928.

New Jersey

State taxes:

Franchise tax[1]

Property tax[2]

[1]Tax Laws, 1926.
Tax is 1-10 of 1 per cent on capital stock issued and outstanding up to $3,000,000. However, it does not apply when 50 per cent of the stock of a manufacturing concern is invested in the state.

[2]New Jersey Tax Laws, 1926.
The state is allowed to levy a limited tax for roads, bridges, and tunnels, soldiers' bonus, and institutions. Taxes are levied on tangible property only. The franchise is not taxed.

North Carolina

State taxes:

Franchise tax[1]

Rate: 1/10 of 1 per cent on value of issued and outstanding capital stock, surplus, and undivided profits

Income tax[2]

Rate: 4½ per cent on entire net income

[3]Revenue Act, 1927.
[2]*Ibid.*

Tennessee

State taxes:

Excise tax[1]

3 per cent on net earnings from sales within the state

Property tax[2]

20 per cent on the $100 valuation

[1]*Annotated Code of Tennessee*, Supplement of 1926.
(In the calculation it was assumed that one-half of the sales were made to buyers within the state. This is purely arbitrary.) There is a franchise tax, which would be $100, but it may be deducted from the excise tax, consequently it is not included.

[2]Director of Finance, Knoxville Chamber of Commerce Dec., 1927. Also C. E. Rightor *National Municipal Review*, Dec., 1927.

South Carolina

State taxes:

Income tax on corporations[1]

4 per cent on entire net income; measured the same as for the Federal Government

Franchise tax[2]

2 mills on each $1.00 of capital stock

Property tax[3]

Rate: 5¼ mills

[1]Income Tax Act of 1926.

[2]*Report of New York State Tax Commission*, 1926.

[3]*Report of South Carolina Tax Commission*, 1926. This report gives the average county tax to be 19.11 mills; the average school tax is 22.85 mills.

Massachusetts

State taxes:

Excise tax[1]

a. $5.00 per $1,000 of vaule of corporate excess[2]

b. 2½ per cent of net income

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[1]General laws relating to taxation and assessment, 1927.

[2]*Ibid.* To ascertain the corporate excess, deduct the local assessment of real estate and machinery from the fair value of the capital stock, consisting of capital stock, surplus, and undivided profits.

INHERITANCE AND ESTATE TAXES

C. P. Spruill, *University of North Carolina*

(Report made to the State Tax Commission and reprinted with the permission of Professor Spruill and the Commission.)

I. Summary of development in the United States
   - A. Death taxes imposed by the Federal Government
   - B. Death taxes imposed by the states
   - C. Death taxes imposed by North Carolina

II. Analysis of receipts from the North Carolina inheritance and estate taxes
   - A. Inheritance and estate tax receipts compared with receipts from other taxes collected by the State Department of Revenue
   - B. Productivity of the death taxes
     1. Large estates *vs.* small estates
     2. Residents *vs.* non-residents
     3. Direct heirs *vs.* collateral heirs and strangers
     4. Inheritance tax *vs.* estate tax
   - C. Burdensomeness of the death taxes

III. Suggested changes in the imposition of inheritance and estate taxes
   - A. Inheritance tax *vs.* the estate tax
     1. Retain the inheritance tax, but raise the rates so as to produce taxes slightly above the present total amount of inheritance tax receipts
     2. Amend the North Carolina estate tax so as to remove its independent character. Provide instead that a tax shall be imposed equal to the excess, if any, of the Federal credit over the amount of the North Carolina inheritance tax. Specify that the credit referred to shall be that of the Federal Estate Tax of 1926 so long as it shall be in force and that thereafter it shall be that credit for payment of death taxes to the states which may be provided by act of Congress.
   - B. Treatment of intangible personalty of non-residents: adopt reciprocity
   - C. Exemptions
     1. Raise the exemption allowed to the widow from $10,000 to $15,000 and the exemption to each minor child from $5,000 to $7,500
     2. Provide that when a share of an estate is transferred to any individual to whom an exemption is allowed the amount of the exemption shall be diminished by one hundred dollars for each one hundred dollars by which the value of the shares transferred exceeds fifty thousands dollars
   - D. Treatment of insurance payable at or after death of the insured
     1. Proceeds of insurance policies are now taxed by North Carolina if paid to the estate of the insured.

2. It is suggested that payments to individual beneficiaries upon the death of the insured should be subjected to the inheritance tax.

   The present discrimination in favor of insurance might be removed entirely by treating payments of insurance like the transfer of other property to beneficiaries of the decedent, but to protect needy dependents only the excess of the total amount of insurance carried by the decedent above $10,000 might be included in the taxable inheritances.

E. Closely repeated successions: provide that the transfer of property from direct heirs to direct heirs, which has been subject to the inheritance tax of North Carolina within a period of three years, shall be taxed only to the extent, if any, that the prevailing rates exceed the rates in force at the time of the next preceding transfer.

IV. Administration

A. Present organization

1. The method of administration in North Carolina
2. The cost of collection

B. Prevention of avoidance and evasion

1. Conveyance of property in North Carolina by non-resident owners to foreign corporations in order to avoid the tax imposed by this state may be reduced by

   a. Providing that incorporation under such conditions within three years prior to death shall, in the absence of proof to the contrary, be deemed a conveyance in contemplation of death and, therefore subject to the tax.

   b. Fixing the schedule of inheritance tax rates so that the excess of the tax imposed by this state above an amount equal to 80 per cent of the Federal estate tax shall not be sufficient to make withdrawal of property from the jurisdiction of North Carolina worth the effort.

2. To prevent possible failure to list bearer securities: require that on the occasion of death of a tenant of a safe-deposit box the bank or safe-deposit company shall withhold the contents of the safe-deposit box from the administrator or executor and from any co-tenant during a period of ten days or until a representative of the State Department of Revenue can be present to secure an inventory of the contents. It should be provided, however, that a deed to a cemetery lot and the will may be withdrawn.

SUMMARY OF DEVELOPMENT IN THE UNITED STATES

The summaries shown below indicate that taxes levied upon the occasion of death have had a long and varied development in the United States. With the exception of the stamp duties upon legacies and successions which were in force from 1798 to 1802, the Federal Government has made effective use of such taxes only during the periods of the Civil War, the Spanish American War, and the World War. Pennsylvania, in 1826, was the first state in the Union to impose an inheritance tax. It was a collateral tax from which parents, surviving spouse, and lineal descendants were entirely exempt. Transfers to direct heirs were taxed first in 1855 by North Carolina. Since the state abandoned that source of revenue in 1874, the similar tax imposed by New York in 1891 is better known. The willingness of North Carolina to apply inheritance taxes seriously, which was illustrated in 1855 by the tax upon direct shares, has manifested itself in more recent times. The rates provided by the Act of 1901 were more heavily progressive than those of any other state. Again, in 1927 North Carolina was the first, and it has remained the only, state to impose an estate tax equal to the Federal credit in addition to the state inheritance tax.

Death Taxes Imposed by the Federal Government[1]

A. Stamp duties upon legacies and successions
   1. Enacted July 6, 1797
   2. In effect from July, 1798, to the repeal on April 6, 1802

B. Act of 1861
   1. Tax upon transfer of personal property only, with progression according to the degree of kinship
   2. It was a mild, slightly regressive probate duty

C. Acts of 1864, 1865, and 1866
   1. Increase of rates
   2. Inclusion of real property

D. Repeal of the inheritance tax in 1870 and the probate duty in 1872

E. Such taxes were upheld by the United States Supreme Court in 1874 (*Scholey* v. *Rew,* 23 Wall. 331, 346)

F. The Income Tax Bill of 1894 taxed inheritances as an element of income (This collapsed when the tax was declared unconstitutional)

G. 1898
   1. Tax upon transfer of personal property only, with progression by totality based on size of the estate rather than upon the individual shares
   2. Upheld by the Supreme Court in 1900 (*Knowlton* v. *Moore,* 178 U. S. 41) except the basing of exemption and progression upon the size of the estate of the individual shares
   3. Repealed in 1902

H. 1916

[1]Shultz, William J., *The Taxation of Inheritance,* 1926.

1. Tax upon the transfer of the estate, not the distributive shares, with the progression according to the amount ranging from one per cent to ten per cent

I. Increases of rates in March and October, 1917

J. 1918
1. Rates in lower brackets were reduced
2. Proceeds of insurance were made subject to the tax
3. An important incidental effect was a burden upon residuary legatees unless prevented by definite arrangement otherwise

K. 1924
1. Increase of rates
2. Credit of the inheritance tax imposed by the states up to a maximum of twenty-five per cent of the tax
3. Gift tax, which was dropped in 1926

L. 1926
1. Reduction of rates and increase of the exemption
2. Credit toward state taxes raised to eighty per cent
3. Retroactive provision for refunding taxes collected under the excess rates of the Act of 1924

Death Taxes Imposed by the States

1. Collateral tax, Pennsylvania, 1826
2. Tax direct shares, North Carolina, 1855, discontinued in 1874
3. Carefully drawn and well administered law of New York taxing collateral shares, 1885
4. Tax upon direct heirs, New York, 1891
5. First law with progression according to the size of the estate Ohio, 1894. It was declared unconstitutional by the Courts (*State* v. *Ferris,* 53 Ohio St. 314, 340)
6. Missouri's law of 1895 with the progressive rates upon collateral shares was declared unconstitutional (*State* v. *Swiltzler,* 143 Mo. 187, 333)
7. Illinois' law of 1895 taxing
   (a) Collateral shares progressively
   (b) Stock of a foreign corporation passing to a non-resident when such a corporation had property or income in Illinois. This was upheld by the Courts (*Magoun* v. *Ill. Trust and Savings Bank,* 170 U. S. 283)
8. Washington, 1901, applied progressive rates according to the amounts of the shares and to the degree of the kinship in the case of collateral beneficiaries, but a proportional rate of one per cent was provided for direct heirs
9. North Carolina in 1901 applied this double progression both to the direct and collateral beneficiaries, but confined to personal property
10. Wisconsin law of 1903
    (a) Double progression applied to both real and personal property
    (b) Progression was by bracket instead of by totality

(c) Exemptions were graduated according to the degree of kinship of the beneficiaries

11. Louisiana between 1903 and 1908 provided for a tax upon transfer of all personal property physically in the State of Louisiana, including securities, deposit credits, etc.
12. Efforts to avoid double and multiple taxation
    (a) 1904, West Virginia and Vermont provided that when inheritance taxes had to be paid to the other states upon the estate of a resident decedent such taxes should be deducted from the amount paid to the state of *domicile*
    (b) 1907, Massachusetts adopted a similar provision and enacted the first measure for fiscal reciprocity in inheritance taxation in this country
13. The first combination of inheritance tax and estate duty was enacted by Rhode Island in 1916

Death Taxes Imposed by the State of North Carolina

A. Act of 1847, Chapter 72
    1. One per cent on collateral shares of decedent's property
    2. Exemption of $300 of real estate and $200 of personal property
    3. Gifts to defeat the act were declared void
B. Act of 1855, Chapter 37
    1. Discrimination between different classes of collateral heirs
    2. Direct heirs were taxed at one per cent. This was the first instance of taxing the shares of lineal descendants in American tax laws
    3. Discontinued in 1874
C. Act of 1897, chapter 168
    The inheritance tax was re-established and was extended to the transfer of personal property to direct heirs.
D. Act of 1901, chapter 9
    1. Applicable to transfer of personal property only
    2. Progression according to both
        (a) Amount of the share and
        (b) The degree of kinship, direct and collateral heirs included
    3. Rates were more radically progressive than those of any other state
E. Act of 1903, chapter 147
    Progression according to the amount of property was removed except for the more distant relatives and strangers
F. Act of 1907, chapter 256
    Rates of 1903 were extended to real property
G. Act of 1913, chapter 201
    Progression according to the amount transferred was abandoned entirely
H. Act of 1915, chapter 85
    Return to mildly progressive rates
I. Act of 1919, chapter 90
    Taxes on securities of a foreign corporation upon basis of the propor-

tion of the value of the property in the state to the value of all the property of the corporation. This was overruled later by the decision in the case of *Rhode Island Hospital Trust Co.* v. *Doughton*

J. Act of 1925, chapter 101

Increase of rates

K. Act of 1927, chapter 80

In addition to the inheritance tax, there was imposed an estate tax equal to 80 per cent of the Federal estate tax of 1926.

Analysis of Receipts from the North Carolina Inheritance and Estate Taxes

The place of the inheritance and estate tax in the system of taxes in the state:

Death taxes in North Carolina are overshadowed by the income tax and the privilege taxes. They stand less far beneath the aggregate of the license taxes. Table 154* summarizes the position of inheritance taxes in comparison with the other groups of taxes collected by the Department of Revenue during the fiscal years 1923 to 1928, inclusive.

Inevitably the tax collections which are dependent upon the value of property passing at death must vary from year to year. Even if the same system of rates were retained, the amounts of taxes payable would depend upon uncertain variables. The value of property left at death, the location of such property within or without the state, the amounts bequeathed to religious, charitable, or educational institutions, and the degree of kinship of the distributors to the deceased influence the amount of the tax and make uniformity impossible.

Taxes upon large estates compared with taxes upon small estates:

Table 155 shows the distribution of tax payments upon inheritances and estates for the year 1927-1928. Table 156 indicates in the same way the distribution of tax payments upon inheritances for the year 1926-1927.

On account of the system of exemptions and progressive rates, the greater part of the tax receipts is derived from the transfer of the large estates. In 1927-1928 there were 1,871 estates on which the total taxes paid to North Carolina amounted to $710,620. Of the total number of estates, 90.38 per cent were subjected to a tax of less than $50,000. Payments by them constituted only 17.85 per cent of the total tax payments. On the other hand, the remaining 180 estates which were subjected to a tax of $500 or more constituted merely 9.62 per cent of the total number of estates but supplied 82.15 per cent of the total tax payments. During the preceding year, 1926-1927, 2,095 estates provided $824,541 of inheritance taxes. Less than $500 was paid on 1,897 of the estates. Although they made up 90.55 per cent of the total number, the taxes paid on them represented only 15.86 per cent of the total tax payments. The

*Editor's Note: The supporting tables, which appear in the *Report of the North Carolina Tax Commission*, have been omitted here because of lack of space. The references have been retained for the benefit of those who have access to the *Report*.

198 larger estates on which $500 or more was paid were 9.45 per cent of the total number and supplied 84.14 per cent of the total tax payments.

Taxes upon estates of residents compared to taxes upon estates of non-residents:

Tables 155 and 156 show also the relative importance of receipts from the transfer of estates owned by residents and non-residents. In 1927-1928 the estates of residents constituted 91.61 per cent of the total number and paid only 87.79 per cent of the taxes collected, while non-residents' estates made up 8.39 per cent of the total number and paid 12.21 per cent of the taxes. Similarly during the preceding year, 1926-1927, the estates of residents were 92.22 per cent of the total number and paid 88 per cent of the inheritance taxes. Estates of non-residents represented the remaining 7.78 per cent of the total number, yet they made 12 per cent of the total tax payments.

Receipts from the inheritance tax compared to receipts from the estate tax:

The estate tax has been in force during only one complete fiscal year, 1927-1928. The total collections of that year on account of both inheritance and estate taxes, excluding the penalties on bad checks, were $710,620. This total was secured as follows:

Inheritance taxes,	$663,201, or	93.33 per cent of the total
Estate taxes,	47,419, or	6.67 per cent of the total
Total	$710,620	100.

If the state should eventually collect the additional estate taxes payable for 1927-1928, the payment of which has been delayed by litigation, the total of estate taxes might be increased by as much as $25,000.

Taxes upon transfers to direct heirs compared to taxes upon transfers to collateral heirs and strangers:

Table 157 summarizes the tax payments upon estates with net taxable value of $100,000 or more during the year 1925-1926. The shares of children supplied the bulk of the receipts, 81.27 per cent of the total. The shares of all direct heirs, including children, provided 87.85 per cent of the total collections from this group of estates. Transfers to collateral heirs and strangers supplied only 11.99 per cent of the total collections from the group.

The preponderance in North Carolina of inheritance tax payments upon the shares of direct heirs is in line with the experience of other states. A committee appointed under the auspices of the National Tax Association reported to the Second National Conference on Inheritance and Estate Taxation that ". . . about 85 per cent, approximately, of all death taxes was paid by people receiving money in the direct line."[2]

The burdensomeness of the inheritance tax:

From a superficial or prejudiced survey of the progressive rates of inheritance and estate taxes it is easy to be persuaded that they are fearfully destructive of capital at the very time that it is needed most by the sorrowing family of the deceased. Closer examination, however, reveals the fact that

[2]*Proceedings of the Second National Conference on Inheritance and Estate Taxation*, 1925, p. 28.

the proportion of the tax to the value of the estate is often not so formidable. In Table 157 it is shown that 71 estates with a net taxable value of $100,000 or more were taxed by North Carolina in 1925-1926. Those estates had an aggregate taxable value of $25,577,355.64. The total inheritance taxes paid to North Carolina upon the transfer of that property amounted to $532,469.93. Comparison of the aggregate taxable value and the amount of the taxes indicates that the total taxes represented only 2.08 per cent of the taxable value. Of course, in the case of the larger estates, the percentage of tax to taxable value was much higher. It is the purpose of progressive rates to make it higher, a purpose which is supported by the principle of progressively greater ability to pay. In the case of the smaller estate the percentage is smaller, but the average, 2.08 per cent, suggests that hardly more than the income for six months was paid to the state on the occasion of successions to property amounting to more than twenty-five and one-half million dollars.

The Inheritance Tax Compared with the Estate Tax

The estate tax, imposed by Section 6 of the North Carolina Inheritance and Estate Tax Law of 1927, has aroused more discussion than any other provision of the statute. As interpreted by the supreme court of the state in the case of *Hagood* v. *Doughton*[3] during the spring term, 1928, this tax is a net addition to the state inheritance tax.

Table 167 summarizes the practice of the various states in the use of an inheritance tax, an estate tax, or a combination of the two. Study of that summary will indicate that twenty-seven states apply the inheritance tax only, that two states have an estate tax only, that Georgia imposes an estate tax upon resident decedents and an inheritance tax upon non-residents, and that fifteen states employ both the inheritance tax and the estate tax.[4] North Carolina is in the last group. Its position in that group is unique. This state alone has attempted to impose an estate tax equal to 80 per cent of the Federal estate tax as a net addition to its inheritance tax and entirely independent of the inheritance tax. It is true that Oregon levies an estate tax[5] in addition to its inheritance tax, but the amount of its estate tax upon the extremely large estates does not equal 80 per cent of the Federal tax. Furthermore, its inheritance tax does not apply to transfers to direct heirs. The thirteen other states in the group impose the estate tax merely to secure the difference between the state inheritance taxes and the amount of the credit allowed under the provisions of the Federal estate tax. Some of these thirteen states, such as Maine and Virginia, provide specifically that their estate taxes shall become void upon repeal of the Federal estate tax by the government of the United States. The effect of the use of both the inheritance tax and an estate tax equal to the Federal credit is shown in Tables 159-163, inclusive.

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[3]Appeal to the Supreme Court of the United States makes impossible a final interpretation of the law at the present time (September, 1928).

[4]The three states remaining—Alabama, Florida, and Nevada—have neither inheritance nor estate taxes.

[5]In form this is an estate tax, but the courts of Oregon have held it to be a succession tax on the ground that it is prorated among the beneficiaries.

In the list of states arranged according to the amount of death taxes imposed upon certain estates, North Carolina stands twenty-first in the case of an estate of $50,000, seventeenth in the case of the $200,000 estate, sixth in the amount of taxes upon a $1,000,000 estate, second at $3,000,000, and first at $4,000,000 and above. If the estates were assumed to be distributed differently—among collaterals and strangers, for example—the relative position of North Carolina would not always be the same as in the case of equal division between a widow and a child, which is the basis of this comparison. The rising rank of the state with increasing value of the property transferred does illustrate, however, the consequences of applying progressive inheritance tax rates and additional progressive estate tax rates to a single aggregate of property passing at death.

The estate tax receipts have not yet been sufficient to compensate for the irritation of taxpayers and the unfavorable publicity which has issued in growing volume from inheritance tax services, protective agencies, and the public press. It was noted in the analysis of North Carolina's tax collections that the amount received from the estate tax during the year 1927-1928 was slightly more than forty-seven thousand dollars, which represented only 6.67 per cent of the total inheritance and estate taxes for the year. If subsequent collections should increase the estate tax for that year by as much as twenty-five thousand dollars the estate tax would be merely 9.84 per cent of the increased total collections.

Instead of continuing the use of two independent taxes payable at death, it seems preferable to the writer that one or both should be modified so as to provide a unified and consistent method of taxation. The relative merits of the estate tax and the inheritance tax have been compared as follows:[6]

Estate Tax

A. Advantages
   1. Simplicity and speed
      a. One set of rates
      b. No investigation of the beneficiaries
      c. Saving of time and expense, both to the estate and the government
      d. The testator can usually determine in advance the total tax and thus provide for exact division of net amounts among the various beneficiaries[7]
      e. No difficulty with life estates and remainders
   2. A step in the direction of harmonizing the death taxes of the states to each other and to the Federal Government
   3. Greater revenue, since when the individual shares are taxed the rates on the higher brackets cannot be applied so far as upon the entire estate

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[6]From the *Report of the National Committee on Inheritance Taxation* to the National Conference on Estate and Inheritance Taxation, 1925, pp. 34-39; and William J. Shultz, *Op. cit.*

[7]Can market value be anticipated so precisely?

B. Disadvantages
   1. Less precise adjustment of the tax to the ability to pay of the beneficiaries of the estate, on account of the absence of progression according to the degree of relationship
      a. The effect of low rates upon direct heirs and dependents ordinarily provided by an inheritance tax can be secured in an estate tax by
         (1) Liberal exemptions. These, however, would benefit collaterals and strangers as well, unless they were determined by
         (2) Exemptions computed according to the number and degree of kinship of the beneficiaries to the decedent
      b. Inequality of the tax upon estates of equal size, some of which pass to a few beneficiaries and others to many beneficiaries. But, under either estate or succession taxes, the testator can control the distribution of the tax among the beneficiaries.

Inheritance Tax

A. Advantage
   1. Theoretically greater fairness on account of more precise adjustment of the tax to the principle of ability to pay
   2. It is the prevailing form among the states. It is thus an old tax which which would seem to be less disturbing to the public than imposition of the same burden in a new form
      a. But the federal estate tax is now an old tax also
      b. The persons subject to the tax are likely to be more interested in the effect of the tax than in its form

B. Disadvantages
   1. Greater complexity
      a. More varied base
      b. Problem of appraising, for the purpose of the tax, life estates and remainders

The National Committee on Inheritance Taxation reported to the National Conference on Estate and Inheritance Taxation at New Orleans in 1925 that the weight of the argument was on the side of the estate tax. But the care with which that conclusion was reached and presented has not been sufficient to influence the force of accepted ideas and long usage, which sustains the inheritance tax in the legislatures of all but three of the states that impose death taxes.

If it were possible to make an entirely fresh start, it may be that the advantages of the estate tax would secure its adoption. In the absence of that possibility, it is probable that the fact that the inheritance tax is the older and the prevailing form among the states, that the administrative machinery is adjusted to its application, and that it makes possible higher rates upon shares passing to remote kin and strangers, justify continued use by North Carolina. It is suggested, therefore, that the inheritance tax be retained. The amount

of revenue now collected from both the inheritance tax and the estate tax can be secured from the inheritance tax alone by raising the rates slightly and by making the progression more rapid and more sustained. For example, the rates upon transfers to beneficiaries in Class A might be raised:

From the present schedule	Per cent
First $25,000	1
Excess over $25,000 up to $100,000	2
Excess over $100,000 up to $250,000	3
Excess over $250,000 up to $500,000	4
Excess over $500,000 up to $1,000,000	5
Excess over $1,000,000	6

To a higher schedule such as that imposed upon direct heirs by New Jersey	Per Cent
First $50,000	1
$ 50,000 to $ 100,000	2
100,000 to 150,000	3
150,000 to 200,000	4
200,000 to 300,000	5
300,000 to 500,000	6
500,000 to 700,000	7
700,000 to 900,000	8
900,000 to 1,100,000	9
1,100,000 to 1,400,000	10
1,400,000 to 1,700,000	11
1,700,000 to 2,200,000	12
2,200,000 to 2,700,000	13
2,700,000 to 3,200,000	14
3,200,000 to 3,700,000	15
Excess over $3,700,000	16

A single schedule of rates producing a given amount of taxes would occasion less irritation than the application of two separate death taxes yielding the same amount of receipts. Just where the rates should be fixed can be decided best by those who combine careful study with long experience. The State Department of Revenue is prepared to submit a schedule of rates which will combine simplicity of operation with productivity of returns. The level of rates should be high enough to yield an important part of the state's tax receipts, but not so high as to discourage unduly the things taxed. Taxes should not be applied roughly with the closed fist but deftly with sensitive fingers.

In view of the great safeguard of state receipts from inheritance taxes which is offered by the credit to the Federal Estate Tax Law of 1926, it appears desirable to impose a tax which in every case will secure for North Carolina the benefit of that provision. While it seems equitable and expedient to remove the independent character of the North Carolina estate tax, it may

not be wise to repeal it altogether. The state inheritance tax may be devised so as to take full advantage of the Federal credit in every anticipated case. Yet, to provide against an unexpectedly large estate and against the possible increase of the credit, it is suggested that the North Carolina estate tax be amended so as to impose an estate tax equal to the excess, if any, of the amount of the credit to the Federal estate tax allowed by the United States for death taxes paid to a state. It should be provided further that the credit referred to shall be that of the Federal estate tax of 1926 so long as it shall be in force and that thereafter it shall be that credit for payment of death taxes to the states which may be granted by act of Congress.

TREATMENT OF INTANGIBLE PERSONAL PROPERTY

At the present time North Carolina imposes a tax upon the transfer at death of all the intangible personal property of a resident of this state. The practice is in harmony with the familiar and generally applied principle that intangible personalty is taxable by the state of residence of the deceased owner. In addition, the state taxes those securities owned by non-residents which were issued by any state or municipal authority within North Carolina or by any company incorporated in North Carolina. The taxation of transfers of securities of domestic corporations owned by non-resident decedents has been defended by reference to the jurisdiction a state has over corporations that have their legal location within it. The power to tax is clear and has been widely used. Indeed, this taxation according to corporate location has been, and still is, one of the most effective sources of double and multiple inheritance taxes. The inequalities that have grown out of tax laws enacted by sovereign states and applied by them to property which often transcends their limits have occasioned a long series of technical and popular discussions. The glaring multiplicity of state inheritance taxes, which has been given sensational publicity, appears to some students of the problem to have so impressed public opinion as to threaten the continued use of a valuable and potentially fair tax. Recognizing the need for greater uniformity and fairness, many of the states have attempted to bring order out of the chaos of death duties. The courts have also exercised a leveling influence, usually as a result of actions brought by representatives of estates the size of which justified the resort to litigation. Legislative experiments include taxation at a flat rate, retaliatory laws, exemption, reciprocal agreements, and a certain measure of Federal control.

In September, 1928, the policy of the several states with reference to intangible personalty of non-residents was as follows:

(1) Three states—Alabama, Florida, and Nevada—and the District of Columbia had no tax payable on the occasion of death.

(2) Eight states exempted such transfers: Colorado, Delaware, Massachusetts, New Jersey, Rhode Island, Tennessee, Vermont, and Virginia.

(3) Twelve states had concluded agreements providing that each state would exempt from its tax the transfer of domestic securities owned by the

decedents resident in any other state in the group or resident in a state which entirely exempted such property: California,[8] Connecticut,[8] Georgia, Illinois, Maine, Maryland, Mississippi, New York, New Hampshire, Ohio,[8] Oregon,[8] and Pennsylvania.

(4) Four states did not generally tax intangible personalty of non-residents but were not entitled to reciprocity; Idaho, New Mexico, Nebraska, and Wyoming.[9]

(5) Twenty-one states taxed such transfers: Arizona, Arkansas, Indiana, Iowa, Kansas, Kentucky, Louisiana, Michigan, Minnesota, Missouri, Montana, *North Carolina,* North Dakota, Oklahoma, South Carolina, South Dakota, Texas, Utah, Washington, West Virginia, and Wisconsin.

(6) Five states taxed the transfer of intangible personalty of non-residents at a flat rate, provided the tax was not superseded by the reciprocal agreements: California, 2 per cent; Connecticut, 2 per cent; Kentucky, 2 per cent; New Hampshire, 2 per cent; and New York, 2 per cent on the gross estate or 3 per cent on the net estate. New York provided further that the tax on a non-resident should not exceed that which would be levied upon a corresponding estate of a resident.

Taxing the transfers at a flat rate, often called the Matthews two per cent plan, has the advantage of simplicity, saving of delay, and reduction of expense both to the tax collector and the estate. The experience of New Hampshire disclosed the fact that the simplicity of operation of a flat rate can be secured without substantial deviation from the amount collected from progressive rates. The two per cent rate applied proportionally was ". . . almost exactly the average rate which residents of the state were paying under the inheritance tax law, after giving credit for all exemptions and deductions."[10]

Both exemption and reciprocity would to some extent meet the desire of a state to attract capital. Opponents of death taxes often represent investment capital as a "shy bird, the cosmopolitan bird, having no country, but building its nest where it can best find security."[11] Undoubtedly the tax system of a state is one of the factors in the determination of the location of industrial plants and in the choice of a home. In certain cases—possibly important cases—it may be the most decisive factor. But it is not the only influence upon the development of industry or the establishment of personal residence. Furthermore, it is possible that part of the shouting for repeal of the North Carolina estate tax has come from persons more interested in reducing the tax upon the transfer of property which they will not remove from the state than in the investment of northern capital within North Carolina. The appeal to self-interest is persuasive, yet before repealing part or all of a particular tax it is well to inquire carefully into the interest of the state. Granting that the

[8]California taxes the transfer of stock of domestic corporations owned by non-residents and Connecticut taxes stock and registered obligations of national banks within the state and domestic corporations when transferred from a non-resident. Ohio and Oregon allow no reciprocity with states which have no inheritance tax laws.

[9]Wyoming is listed by Ohio as being entitled to reciprocity.

[10]*Proceedings of the National Tax Association.* Vol. XVIII (1924), part 2, p. 47.

[11]William J. Shultz, *op. cit.,* p. 321, quoted from Soward and William, *Taxation of Capital,* p. 150.

attraction of investment is desirable and that low taxes are inviting, it must be remembered that unless expenditures are reduced a decrease of the rate of one tax must either secure as great or greater receipts through the growth of taxables attracted by the low rates, or must be followed by increase of other taxes. If it should develop that other taxes had to be raised, then either the capital subject to those taxes would be repelled or, if they were not imposed upon investment capital, the burden would have to be borne by the other taxpayers of the state. It is evident also that additional investment in North Carolina is not an absolute gain. More capital and more people occasion larger expenditures. Presumably the greater economic productivity and greater tax capacity exceed the attendant social and fiscal costs, but measurements are uncertain and only when they do exceed the costs is there a net gain to North Carolina. Considerations less buttressed by popular prejudice but built upon secure foundations are those of simplicity, uniformity, and justice. It is upon those grounds that exemption or reciprocity may be urged most effectively.

Exemption is the simplest and speediest method of dealing with the transfer of property of non-residents. As shown above, it has been adopted by eight states, including Massachusetts, New Jersey, Delaware, and Virginia. Securities issued under the authority of those eight states are not taxed by them when such securities pass at the death of a non-resident owner. If North Carolina were to adopt this policy, it would refrain from taxing the transfer of securities issued under its authority when owned by a non-resident decedent. By this step it would gain for citizens of North Carolina immunity from taxes upon the transfer of securities issued by corporations or governmental agencies under the jurisdiction of the twelve reciprocal states. North Carolina would exempt the transfer of its securities owned by residents of all other states, but residents of North Carolina would be subject to death taxes upon securities issued under the authority of twenty states. In this respect absolute exemption is less advantageous than reciprocity. Exemption releases non-resident decedents from the tax upon intangible personalty freely and without any effort to secure a similar benefit for residents of this state. Reciprocity, on the other hand, would provide an exemption only for residents of those states which allow exemption for residents of North Carolina. By withholding exemption from residents of states which continue to tax the transfer of intangible personalty of non-residents, North Carolina would add its influence to the effort to secure uniformity without any uncompensated sacrifice of the interest of its citizens.

Exemption and reciprocity are advantageous to:

1. Non-resident decedents owning North Carolina securities.
2. Resident decedents owning securities of foreign corporations incorporated in states having reciprocal or absolute exemption legislation, since those other states would not tax them.
3. State income and corporation taxes, local general property taxes, and communities in the state to the extent that new capital is attracted or removal of existing capital is avoided.

4. Sale of bonds by local governments.
5. Inheritance tax receipts to the extent, if any, that more property is accumulated and subsequently taxed at death.

They are disadvantageous to:

1. State inheritance tax receipts to the extent that securities otherwise taxable would be exempted. This may be offset in part by raising the rates so as to take for North Carolina part of the taxes upon residents of this state which are now imposed by the reciprocal states and from which those residents of North Carolina would be relieved if reciprocity were adopted.
2. Payers of *other taxes* to the extent that such taxes have to be increased to make up for loss of inheritance tax receipts.

Precisely what amount of revenue would be lost as a result of adopting exemption or reciprocity cannot be determined. The reduction of taxes which would follow renunciation of this source of governmental income would depend upon unpredictable deaths of non-residents possessed of intangible personal property taxable by North Carolina. Estimates based upon experience of the past two years indicates that absolute exemption would occasion a loss to the state treasury of about fifty thousand dollars.[12] The sacrifice incident to reciprocal exemption of intangible personalty would be less on account of the fact that the exemption would extend only to twenty-three states and the District of Columbia. During the two years 1926-1927 and 1927-1928 the loss would have been not more than forty thousand dollars,[12] possibly not more than thirty-five thousand dollars. Of course, if the number of exempting or reciprocal states were to increase, there would be a corresponding increase of the immediate loss of tax receipts.

The questions at issue, then, are: (1) as a matter of principle, should a state tax the transfer at death of personal property owned by a resident of another state? (2) As a matter of self-interest, would the indirect gains to North Carolina exceed the certain loss of unpredictable amounts of inheritance taxes?

The following are examples of legislative statutes authorizing reciprocal exemption of intangible personalty of non-residents:

> Reciprocal Statute of Georgia, Act Number 331, Section 5, Approved August 20, 1927.
> "Be it further enacted by the authority aforesaid that the tax[13] imposed by this Act on personal property (except tangible personal property having an actual situs in this state) shall not be payable if the laws of the state of residence of the decedent at the time of his death exempted residents of this state from transfer taxes or death taxes on such property."
> Reciprocal Statute of Maryland, Chapter 350, Laws of 1927, Section 148-A.

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[12]

Fiscal Year	Total	Taxes paid to North Carolina on the transfer of non-residents' estates	
		On Real Property	On Personal Property
1926-1927	$98,956	$45,106	$53,850
1927-1928	86,744	36,243	50,501

[13]The Georgia estate tax.

"Except as to tangible personal property having an actual situs in the State of Maryland, no tax or commission of executors or administrators of non-resident decedents, and no inheritance, estate, or death or transfer tax of any character, in respect of personal property (including also therein mortgages upon real or personal property located within the State of Maryland) of non-resident decedents, shall be payable (a) if the decedent at the time of his death was a resident of a state or territory of the United States, or of any foreign country, which at the time of the distribution, transfer, or other disposition of such personal property of such decedent in Maryland did not impose a transfer tax or death tax of any character in respect of personal property of residents of this state (except tangible personal property having an actual situs in such state or territory or foreign country), or (b) if the laws of the state, territory or country of residence of the decedent at the time of such distribution, transfer or other disposition contained a reciprocal exemption provision under which residents of Maryland are exempted from transfer taxes or death taxes of every character in respect of personal property (except tangible personal property having an actual situs in such state or territory or foreign country) provided the State of Maryland allows a similar exemption to residents of the state, territory or country of residence of such decedent. For the purposes of this section the District of Columbia and possessions of the United States shall be considered territories of the United States. Nothing herein shall be construed to subject to taxation anything heretofore exempt therefrom; and any and all laws or parts of laws of Maryland in conflict or inconsistent with the provisions of this Section 148-A are hereby repealed to the extent of such conflict or inconsistency."

Reciprocal Statute of New York, Chapter 357, Laws of 1926, Article 10-A, Section 248-p.

"The tax imposed by this article in respect of personal property (except tangible personal property having an actual situs in this state) shall not be payable (1) if the transferor is a resident of a state or territory of the United States which at the time of the transfer did not impose a transfer tax or death tax of any character in respect of personal property of residents of this state (except tangible personal property having an actual situs in such state or territory), or (2) if the laws of the state or territory of residence of the transferor at the time of the transfer contained a reciprocal provision under which non-residents were exempted from transfer taxes or death taxes of every character in respect of personal property (except tangible personal property having an actual situs therein), providing the state or territory of residence of such non-residents allowed a similar exemption to residents of the state or territory or residence of such transferor. For the purposes of this section the District of Columbia shall be considered a territory of the United States."

In the event of adoption by North Carolina of either absolute exemption or reciprocity, a considerable saving to estates of non-residents and some economy in the administration of our state inheritance tax might be achieved by statutory approval of the substitute for waiver which has been proposed by Mr. Howard B. Smith.[14] A substitute for waiver simply authorizes the tax authority to permit immediate transfer by the issuing corporation of securities of a non-resident decedent upon receipt of an affidavit showing that the deceased was a resident of a state entitled to exemption. The affidavit should

[14] *Bulletin of the National Tax Association*, Vol. XII, No. 2, p. 41.

be made in duplicate so that one copy may be sent to the state department of revenue and the other to the corporation or the governmental agency transferring on its books the ownership of the securities. By this means the state may simplify the procedure. Corporations may transfer stocks and bonds without waiting for a formal waiver. The administration of estates may be expedited and sometimes hardships upon beneficiaries growing out of delay and shrinkage of values may be avoided. Excessive losses, expense, and delay occur only in extreme cases, but it is in the exceptional cases that relief is most needed. Mr. Franklin S. Edmonds[15] has reported an instance of shrinkage of the value of property in a New York case from $3,471 to $63 during a period of three months intervening between the time of death and the transfer of the securities. The additional examples quoted below illustrate difficulties which sometimes arise and which might be obviated with advantage to estates in process of settlement and without loss to North Carolina.

"In the recent settlement of an estate that had to transfer one share of stock of a railroad company which was incorporated in Maryland and Pennsylvania and which maintained a transfer office in New York, it was necessary to prepare and file three copies of the will, two of which had to be certified; three certified copies of the letters testamentary; two applications under oath for appraisal; six schedules setting forth assets and liabilities; a copy of the petition for letters; a copy of the executor's bond; an order of court; a resolution of the board of directors of the corporate executor; evidence of payment of the transfer taxes; an affidavit of no indebtedness in Pennsylvania; a Pennsylvania short certificate; a New York inheritance tax waiver; a Pennsylvania inheritance tax waiver. And the value of the stock was less than $100 and the tax liability less than a dollar."[16]

Another case was reported by Mr. Davidson of Buffalo, N. Y., to the Preliminary Conference on Inheritance and Estate Taxation. "A woman about fifty-five years old came into our office the other day and said that her brother had died about six months before. Her brother was a bachelor, running a drug store, and had a little surplus money, and he wanted to be absolutely safe, so he would invest only in stocks listed on the New York stock exchange. He died and she was trying to settle the estate. He left about fifty thousand dollars; five thousand dollars to an invalid, and the balance was to be divided between herself and a much older brother; so when she started to try to get this, she said she wanted to sell these stocks so she could pay the five thousand dollar gift and the debts. She said she was getting nowhere, and called to know if we had anyone to tell her what to do. I gave her a list of the requirements from the Prentice-Hall Company, which stated she must get eighteen waivers from the State of New York, and she must deal with fifteen states. She said, 'I wrote to this state, and they told me I could not transfer this stock, until I had paid the debts of the whole estate and settled

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[15] *Ibid.* Vol. XI, No. 9, p. 265.

[16] Edwards, F. S., "The States are Cleaning House, a Survey of Recent Developments in the Taxation of Inheritances," reprinted from *The Outlook* of April 21, 1926; in the *Bulletin of the National Tax Association*, Vol. XI, No. 9 (June, 1926), p. 264.

it up, and sent on certificates to that effect. I wrote back and told them I wanted to sell the stock, so I could pay the debts and settle up.' She said, 'One state wrote to me, after you pay the taxes in these other states, we can figure out how much this tax is'; but she said, 'When I wrote to the others, they told me I first had to pay the taxes in this state over here before they could tell me what it was.'

"That was just an ordinary estate totalling altogether fifty thousand dollars, on which she hoped to get twenty thousand dollars, but to do that she had to deal with fifteen different states and get eighteen waivers from the State of New York."[17]

Another method of avoiding double taxation of intangibles is the allowance of a credit to the inheritance tax payable to this state equal to the sum of taxes paid to other states upon the transfer of property taxable by North Carolina. There is a basic distinction between a credit to the tax and the other agencies of uniformity discussed above. Exemption and reciprocity provide relief for: (1) non-residents who die possessed of securities issued under the jurisdiction of the state, and (2) resident decedents whose foreign securities are freed from transfer taxes imposed by the reciprocal states.[18] Crediting the inheritance tax payable to North Carolina with the amount of taxes imposed by other states upon the transfer of the same property would reduce the payments to this state by both residents and non-residents succeeding to property taxable by North Carolina and taxed by other states. Such a credit would tend also to perpetuate the tax upon intangible personal property of non-residents, for taxpayers are less inclined to object to a policy which diverts receipts from the treasury of their state to that of another than to a system which takes from their own pockets two taxes upon one transfer of personal property. A non-taxing state which allowed this credit to its residents would make easier the tax according to corporate location imposed by other states and would have only the consciousness of virtue and self-sacrifice as its reward.

EXEMPTIONS

To widows and to minor children

The inheritance tax often falls most heavily upon a family suddenly deprived of its sole source of support and succeeding to a comparatively small estate. Recognizing the undesirability of aggravating the difficulty experienced by such a family, all of the states that tax transfers to direct heirs, with the single exception of Pennsylvania, allow some exemptions. North Carolina allows $10,000 to the widow and $5,000 to each minor child. Reference to table 164 will show that eighteen states allow a larger exmption to widows than North Carolina. Eleven states exempt the same amount, and nine states permit

[17]Held in connection with the Seventeenth Annual Conference of the National Tax Association, St. Louis, 1924, p. 77.

[18]Residents of North Carolina are exempted in any case by the eight states that do not tax the transfer of intangible personalty of non-residents. On the other hand, neither exemption nor reciprocity will release residents of this state from the death taxes imposed by the twenty other states of the group to which North Carolina now belongs.

smaller exemptions. The other states, nine in number, do not apply the tax. Table 165 indicates the twenty-two states that allow larger exemptions to minor children than North Carolina. The same amount, $5,000, is provided by six other states, while ten states allow smaller exemptions.

It is suggested that the occasional severity of the tax might be reduced by allowing to a widow $15,000 entirely exempt and to each minor child $7,500. Such an increase would cause a loss of revenue. The loss would not be serious, however, and it would be lessened if the larger exemption to these beneficiaries of small estates were coupled with a "vanishing exemption" to beneficiaries who succeed to large estates. This may be accomplished by providing that when a share of an estate is transferred to any individual entitled to an exemption the amount of the exemption shall be diminished by one hundred dollars for each one hundred dollars by which the value of the share transferred exceeds fifty thousand dollars. Thus a widow succeeding to $25,000 would receive the full exemption of $15,000. Another securing a $60,000 share would be allowed only $5,000 exempt. A third who received $65,000 from her husband's estate would be taxed upon the whole amount without exemption. Possibly the point at which the amount of the exemption begins to diminish should be moved to some lower level such as forty thousand dollars. The "vanishing exemption" has been discussed often,[19] but it has not been adopted by an American state. Belgium included it in the law of October 11, 1919.[19] An analogous but more extreme form is now in effect in Massachusetts. That state provides that if a distributive share exceeds the amount of the exemption the tax shall be computed upon the entire share without allowance of any exemption. If, however, this computation results in reduction of the value of the share below the amount of the exemption no tax is exacted.

To special types of securities

The interest of municipalities and counties in the sale of bonds upon the most advantageous terms has raised the question as to whether the transfer of those bonds should not be exempted from the North Carolina inheritance tax. The practice of the several states is not uniform. Twelve states, including New York, Pennsylvania, and California, tax some securities owned by non-resident decedents, but do not tax the transfer of municipal bonds. Twenty-two states, including Connecticut, Ohio, and North Carolina, tax the transfer of municipal bonds under certain conditions.[20] Without doubt the exemption of such securities would be favorable to their sale. The adoption of exemption or reciprocity with regard to all intangible personal property owned by non-resident decedents would secure for the state substantially all of the advantages of a specific exemption to governmental bonds. Either of those general policies seems preferable to the addition of another special privilege by specific exemptions of a particular class of property.

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[19]William J. Shultz, *op. Cit.*, pp.270-271.

[20]See the *Prentice-Hall Tax Diary and Manual for 1928*, p. 30.

TREATMENT OF INSURANCE PAYABLE AT OR AFTER DEATH OF THE INSURED

North Carolina taxes the proceeds of insurance policies payable to the estate of the insured. It does not tax payments to specific beneficiaries. The Federal Government includes in the taxable estate all insurance payments in excess of forty thousand dollars regardless of whether it is paid to the estate or to named beneficiaries. A tax upon the passing of insurance money to a named beneficiary is imposed at the present time by Wisconsin, Montana, Arkansas, Mississippi, and Tennessee.[21]

The cases decided by the courts have not yet been sufficient to constitute a completely final test of the tax upon such payments. In the case of *State* v. *Allis,* 174, Wis. 527, 184 N. W. 381, the constitutionality of taxing insurance paid to named beneficiaries was sustained. The court held that when the premiums were paid by the decedent directly or indirectly—through wife or child, for example—the tax would accrue. But where "business concerns take out insurance upon lives of employees and officers, the premiums being paid by the concerns, there is no inheritance tax."[22]

The present discrimination in favor of insurance which prevails in most of the states, including North Carolina, has developed because of reasons which are self-evident. There now appear reasons for modifying that discrimination. Insurance payments are made in the most liquid form, cash. Paying the tax would not, therefore, involve the burden of a sacrifice sale. If a policy holder dies before the policy matures, the beneficiaries receive a payment greater than the sum of the premiums. If he dies after maturity of the policy, his dependents have had the benefit of the protection afforded by insurance, and they secure at his death an accumulated investment. In either case there is a definite ability to pay the inheritance tax. There is sometimes an inequality in the burden of the tax which arises from the inability of the productively employed members of the family to secure insurance. If one of two neighbors is an unacceptable risk to the insurance companies and yet by thrift and industry builds an estate in securities and a home amounting to $25,000 at his death, the widow who succeeds to the whole of it must pay an inheritance tax to North Carolina amounting to $150. If the other neighbor lives in a rented house and makes no investment except the purchase of $25,000 of ordinary life insurance payable to his wife in a lump sum, the widow escapes the tax entirely. Such a case would be exceptional, but it may emphasize the question as to why insurance should be treated more favorably than other property left for the maintenance of dependents, or more liberally than other investments.

The more liberal treatment of the proceeds of insurance policies might be removed altogether by treating payments at or after death like the transfer of other property to beneficiaries, but to protect needy dependents it may be provided that only the excess of the total amount of insurance above $10,000 shall be subject to the tax.

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[21] *Commerce Clearing House Inheritance Tax and Stock Transfer Service,* 1926-1928, Vol. I, p. 31.

[22] *Ibid.* Vol. II, pp. 2803-2804.

CLOSELY REPEATED SUCCESSIONS

Occasionally it happens that the frequency of deaths within a family during a short time may cause hardship upon surviving heirs who succeed to property diminished by repeated imposition of the inheritance tax. If a family were to experience an automobile accident causing the immediate death of an aged grandfather, the death of the grandmother fifteen months later, and the death of an adult son two years and a half after the accident, the transfers of a residence from the grandfather to his widow, from the grandmother to her adult son, and from the adult son to a minor grandson would be taxed separately as they occurred. That is, the North Carolina inheritance tax would be imposed three times within less than three years.

In order to avoid excessively frequent imposition of the tax without releasing it from unexpected successions by collateral heirs and strangers, it is suggested that the law be amended so as to provide that the transfer of property from direct heirs to direct heirs which has been subject to the inheritance tax of North Carolina within a period of three years shall be taxed only to the extent, if any, that the prevailing rates exceed the rates in force at the time of the next preceding transfer.

ADMINISTRATION OF THE INHERITANCE AND ESTATE TAXES

Present organization

Since 1921 North Carolina has made use of that method of collecting inheritance and estate taxes which experience of this and other states has proved to be most effective. The State Department of Revenue has complete charge of the administration of these taxes. It employs fifteen deputy commissioners, each of whom is charged with the collection of inheritance taxes, license and privilege taxes, and the income tax in the district of the state to which he is assigned. Three deputy commissioners have general supervision over the local deputies. One is stationed in Raleigh, one in Rockingham, and one in Statesville. Inheritance tax inventories are scrutinized by the inheritance deputy. All of the deputies are responsible ultimately to the Commissioner of Revenue. While the personnel of the collecting force is concerned with taxes other than the inheritance tax and is by no means confined exclusively to it, there is opportunity for the development of specialized knowledge. In addition, the checking of returns and coördination of methods of procedure are promoted by the inheritance tax deputy, who gives the greater part of her time to this work.

Cost of collection

The cost of collecting the North Carolina inheritance and estate taxes in 1927-1928 represented five per cent of the net receipts from this source. In 1926-1927 the cost of collecting the inheritance tax was four and one-half per cent of the net collections.[23]

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Fiscal Year	Office Salaries Field Deputies & Misc. Expense	Clerks' Fees	Total	Net Collections
1927-1928	$29,754	$6,726	$36,480	$710,636
1926-1927	30,594	6,641	37,235	824,541

Note: The totals of office salaries, etc., represent actual outlay without allowance for the budgetary reduction of about twenty per cent on account of receipts from the Automobile Bureau.

The cost of collection in North Carolnia is greater than the two and one-half per cent reported in the case of Wisconsin by the National Industrial Conference Board.[24] It is less than the nine per cent which, in 1924, was the average cost in forty-eight counties of New York.[25] The latter state still retains a relatively decentralized system of collection.

Prevention of avoidance and evasion

A simple and effective method of escaping the North Carolina inheritance tax that appears to be gaining the favor of owners of large properties is to change personal residence from North Carolina to a state which imposes lower rates or none at all and to convey property in North Carolina to a corporation incorporated in that other state. In cases of this kind North Carolina has no jurisdiction over the person of the decedent. Neither can it tax the transfer of stock in a foreign corporation, even though all the productive property which that stock represented might be located in North Carolina.

This tendency may be discouraged slightly by providing that incorporation under such conditions within three years prior to death shall, in the absence of proof to the contrary, be deemed a conveyance in contemplation of death and, therefore, subject to the tax.

It may be prevented more certainly by removing the incentive. That is, so long as the Federal estate tax is in force, North Carolina may fix the schedule of inheritance tax rates so that the tax imposed by this state upon the larger estates shall not exceed the Federal credit by an amount great enough to make worth while the withdrawal of property from the jurisdiction of the state.

A means of evasion which has been detected and checked in some measure by twenty-six states is the failure to list bearer securities among the taxable transfers. If he is so disposed, the representative of a decedent in North Carolina may quietly divide coupon bonds among the beneficiaries and ignore the existence of those securities in making out the inventory for tax purposes. The possibility of evading the tax in this way may be reduced by requiring that on the occasion of death of a tenant of a safe-deposit box the bank or safe-deposit company shall withhold the contents of the safe-deposit box from the administrator and all other persons, including co-tenants, during a period of ten days or until a representative of the state department of revenue can be present to secure an inventory of the contents. It should be provided, however, that the will and a deed to a cemetery lot may be withdrawn under the personal supervision of an officer of the bank or safe-deposit company. A proper penalty should be imposed to insure observance of the enactment.

Twenty-one states impose a requirement similar to the one suggested upon banks and safe-deposit companies with respect to boxes held by both residents and non-residents; Arkansas, California, Colorado, Idaho, Illinois, Indiana, Iowa, Kentucky, Louisiana, Michigan, Minnesota, Missouri, Montana, New Jersey, New York, North Dakota, Ohio, Oklahoma, Oregon, South Caro-

[24] *The Tax Problem in Wisconsin*, p. 118. Quoted by Shultz, op. cit., p. 200.
[25] *Bulletin of the National Tax Association*, Vol. XI, No. 7, p. 196.

lina, and Utah. Five states impose such a requirement with respect to non-resident decedents only: Arizona, New Mexico, Washington, Wisconsin, and Wyoming.

The right of a state to know what property is left in a safe-deposit box, whether held individually or jointly, in order to determine whether a tax is due was sustained in the case of the *National Safe Deposit Co.* v. *Stead*, 250 Ill. 584, 95 N. E., and affirmed in 232 U. S. 58.

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SOME ASPECTS OF MUNICIPAL FINANCE IN NORTH CAROLINA

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North Carolina Municipalities

In a discussion of problems of municipal finance in North Carolina it is well to consider first the North Carolina municipalities themselves. North Carolina had, according to the 1920 census, 413 incorporated places of sub-census size, *i.e.*, of less than 2,500 population, with a large number of places of similar size unincorporated. Twenty-four of the 413 had a population of less than 100; 249 had less than 500; and 333 less than 1,000. There were only 57 census-size cities and towns, *i.e.*, incorporated places with a population of over 2,500, and the largest cities in the state had less than 50,000 inhabitants. Thus North Carolina is still a rural state, though through the present process of industrialization it is rapidly becoming urbanized and will probably have one city or more in the 100,000 class when the next Federal census is taken in 1930.

This process of urbanization has gone on steadily throughout the nation for the last century, until we now have in this country some of the super-cities of the world. This concentration of population in small areas affords opportunities and advantages that are impossible to be had in the smaller population groups, as through large-scale or mass coöperation many things are possible of accomplishment that cannot be realized by smaller or weaker efforts. This is true of economic production, public improvements of various kinds, education, and recreation and cultural advantages. But with all this concentration of population, the life of the urban group becomes more complex and intricate, more unwieldly and hard to control—with corresponding opportunity for exploitation—and also more expensive to operate. The cost of living is higher, problems of health become greater, and individual competition is keener. Consequently, to counteract these handicaps, there has been a slight tendency in recent years toward decentralization, rather than centralization of population. This is especially true in the North where satellite cities are being founded near the larger cities for the establishment of industrial plants. Therefore, it may be considered a timely occasion to compare the advantages and disadvantages of urbanization and decentralization. What are the desired values to be obtained from municipal organization, and in what units of population may they be most effectively achieved? Do the advantages of centralization outweigh its disadvantages, or do the disadvantages of smaller units appear less significant in comparison with the advantages received from a simpler and less complex organization of life? May the disadvantages of the city be eliminated more quickly or can the opportunities lacking in the small town be supplied more easily than corresponding efforts will show in the opposite direction? Is all the emphasis to be placed upon mere quantitative efficiency, or is there also a qualitative element that enters in? Unfortunately, we do not have accurate studies made

for the purposes of comparison. But at any rate, North Carolina is now at the turning of the ways; she has an ample field for study within her own borders and that of the larger cities, and it is for her to choose in which direction she will progress—in the mere quantitative growth or in the qualitative development of her own municipalities.

But first let us consider what is meant by incorporation. As a matter of definition, what is an incorporated town? It is any group of people living in one geographic unit who may wish to organize into a political unit for purposes of receiving advantages which individually and unorganized they are not able to secure. These are, for example, police and fire protection; public improvements, such as streets or sidewalks; electric lights, water, sewerage; better advantages of health, recreation, and education. In North Carolina the requirements for such incorporation, which must be granted on petition to the legislature, are that the incorporation contemplated shall contain fifty persons and twenty-five eligible voters. Whether this is a large enough unit to accomplish any approach toward efficient organization may be challenged, but such, nevertheless, is the law. On the other hand, no incorporation is compulsory. No matter how large the unit of population, the question of local self-government and responsibility is purely voluntary on the part of the people concerned. As a consequence, North Carolina has two manufacturing towns with estimated populations of around 10,000 which are controlled chiefly by corporation interests and which have no legal incorporation whatsoever, but are still, to all intents and purposes, merely parts of the county unit system. Such a situation may also be a challenge to governmental efficiency. However, such a discussion is not within the province of this paper.

To pay for the benefits of incorporation large funds are necessary, and this is the chief problem to be considered in connection with city government. As to the measure of local self-government received through incorporation, the cities and towns in North Carolina have very little, as their powers are limited by law and they are almost entirely under legislative control. This is especially true of finances, bond issues for permanent improvements, etc. The poll tax is limited by the constitution to $1.00, and the general property tax rate is also limited to $1.00 for general purposes, though the latter may be supplemented to cover the amount needed for bond issues. Moreover, the Municipal Finance Act requires that no bonds may be issued "unless the net debt does not exceed 8 per cent of the assessed valuation," except for certain purposes. However, any specific town may secure a special public-local act through the legislature permitting it, as an exception, to violate this law. This is the constant practice of the legislature, which through its inconsistency in granting unlimited special acts—and one is rarely refused—defeats and contradicts its own general law. The question may be well asked: what is the value of having a Municipal Finance Act when, in any case, any city or town so desiring may be given permission to violate its requirements? In fact, in 1925 three towns in North Carolina were allowed by the legislature to incur a

bonded indebtedness amounting to 13, 20, and 28 per cent, respectively, of their assessed valuation, when the law specifically says that it shall be limited to 8 per cent. The same situation also exists in the counties. This is not the case with European cities, where a centralized board of administrative control supervises and directs the administration of the individual cities. Would such a system of municipal government for the states be advisable in this country, or would it not? Would it give more freedom, or less, to the cities and towns? Or would it mean a more efficient and better functioning government than we now possess?

What, then, is the actual situation in respect to financial administration in North Carolina municipalities? As there are only 137 incorporated cities and towns in North Carolina of over 1,000 population, according to the 1920 census, and 72, or over one-half of these, have between 1,000 and 2,000 population, this group was selected for special study. For purposes of comparison the seven largest cities in the state—those having over 25,000 population—were also considered. For various reasons, such as the fact that some of these were merely suburban to others and therefore did not constitute real geographic units comparable to the general group considered, 7 of them were omitted, leaving 65 of the smaller towns with a combined population of about 90,000, and 7 cities with a total population of 225,000, or an average of about 35,000 each, to be studied. Following are some of the facts discovered in regard to these. The figures are those given in the report of the Commissioner of Revenue for the year 1925.

Assessed Valuation

The assessed valuation of real and personal property in the 65 towns studied ranges from about $1,000,000 to $3,000,000, the average assessment per town being around $2,000,000, or about $1,500 per capita, whereas the average assessed valuation per capita for the cities is about $2,500. Of this about 20 per cent in both cases is personal property. It might be stated that the assessments of the cities and towns are made, according to law, by county assessors and are usually at about 70 to 75 per cent of their actual value.

Receipts and Revenue

Great variation is shown in the receipts reported by the various towns. Six report less than $10,000, while 9 report over $100,000. Most of the latter, however, had heavy receipts from bonds or borrowed money. The majority of the towns reported receipts ranging from $30,000 to $70,000, the average being around $60,000 each. Twenty-seven towns reported no receipts from borrowed money. The average revenue per capita, or the average cost of government per individual, in the small town is $45, while that of the city is about $125, though in the case of the latter much of this is paid by the large corporations and not by the individual citizen. But of course the differences in services received must also be taken into consideration, although it would be interesting to know if the corresponding differences in cost are commensurate with the differences in services.

As mentioned above, in three cases the bond issue exceeded the amount allowed by law, which provides that a bond issue may not exceed 8 per cent of the total assessed valuation of property, "unless the bonds . . . are to be funding or refunding bonds, or are bonds for water, gas, electric light or power purposes . . ." (Municipal Finance Act). These special cases may have met the conditions and qualifications specified in the law, although one bond issue amounted to 28 per cent of the assessed valuation of the town and another 20 per cent of the valuation. However, it may also have been that there was a special act authorizing these funds, which it is at all times possible to put through the legislature. Four of the towns had receipts from bonds of over $100,000 (one reporting $300,000 and another $258,000), which in both cases amounted to over 75 per cent of the total revenue for the year.

As to the taxes levied on property, this in most cases constituted less than one-half of the total receipts, the majority of the balance being receipts from bonds or borrowed money. In fact, in the case of the towns, this constituted about one-third of the total, and in the case of the cities about two-thirds. Only one of the seven cities reported no receipts from borrowed money.

The next largest item of receipts was from electric lights and other public service plants, one town receiving over $100,000 from this source, which of course did not include deductions for operating expenses. Fifty-three of the towns reported receipts from this source, 44 of them receiving a net income, and 7 of them realizing a profit of over $10,000. Twenty-five of the towns are reported in McGraw's Central Station Directory as owning municipal electric light plants, though few of them generate their own power and most are merely distributing plants for some of the larger power companies in the state, such as the Carolina Power and Light Company of Raleigh.

Expenditures and Disbursements

The total expenditures of the towns varied greatly throughout the state (as did the receipts), some having heavier payments on bonded indebtedness than others, but practically all of them expending from $1,000 to $50,000 for this purpose. The expenditures also included the expense of operating public service plants, which item in some cases was quite large, constituting an expenditure in one town of over $100,000. This town also showed the largest profit or a net income of $34,000—which happened to be more than the total annual cost of the town government—exclusive of the operating expense of the public service plant.

The total expenditures for the various towns ranged from less than $10,000 in some of the mill towns to over $300,000—one town spending exactly this amount on streets and sidewalks during the year, another $240,000 for the same purpose, and two others over $100,000. In fact, except for payments on bonds, this seems to be the chief item of expenditure made by the towns, and perhaps the bond payments were in most cases also for this purpose, although it would not be possible to secure this information without going through all the special acts in the public-local laws. However, it would be interesting to know whether or not the expenditures of the small towns could be gauged by

the miles of paved streets and sidewalks they possess. This, then, is the item that necessitates the largest amount of expenditure and constitutes the chief burden on the town. A part of this—one-half, according to the Law of Municipal Corporations—is assessed upon the individual property owner, but this is also a form of indirect taxation and constitutes a burden on the taxpayer in addition to the ordinary property tax.

It appears that sixteen of the towns also supplement the school funds supplied by the state for the support of the local school, thus raising the standard of the schools to compare more favorably with those of the city, three towns contributing $10,000 or more to this purpose.

The total expenditures for the towns average around $60,000 each, or about $40 per capita. Those for the cities average about $4,000,000, or about $125 per capita, which are approximately the figures given for average and per capita receipts, the difference being that the city shows better budgeting procedure, as the receipts and expenditures come nearer to balancing each other than do those of the towns.

Approximately one-third of the total disbursements of the towns were for payments on bonds, interest, and other indebtedness, which was also true of the cities. If, as suggested above, a large proportion of this is for street and sidewalk improvements, then a major portion of the town's disbursements goes to this purpose. Since at least the main street through the town serves the county and also the state as well, might it not be feasible or reasonable to expect that the county and state should pay at least a part of this expense and relieve the towns of this their major burden, thus releasing revenue for other services that are lacking or poorly supported? The average expenditure per town towards bonds and other indebtedness is about $20,000 a year, while that of the city is around $1,500,000, or about 35 per cent of the total disbursements in each case.

RECEIPTS AND EXPENDITURES COMPARED

Comparing the receipts and disbursements, we see evident lack of proper budgeting procedure, which is a specific legal requirement for the municipalities in the state. In many cases the expenditures exceeded the revenue received, and often also there was an unnecessarily large balance at the end of the year, which is an almost equally significant sign of poor financing; whereas, if a proper budgeting system had been adopted neither of these results would have been necessary. Of the total 65 towns, 16 failed to provide enough revenue for the town's current expenditures, in which case money had to be borrowed to meet current expenses, which is contrary to law, except for short terms and in anticipation of taxes which have been appropriated for this purpose. If a careful estimate of the needs had been made and taxes levied to meet these, this emergency would not have arisen. It is such practices as these which endanger a town's credit and make it hard to sell bonds when they are issued. Moreover, of the 65 towns, 14 also showed a balance at the end of the year of over $10,000—one town having a balance of over $100,000, an unnecessarily large balance to hold in the treasury, as it meant the imposi-

tion of an unnecessarily heavy burden on the taxpayers, if this amount was not to be needed or used immediately. Some of this may have been applied to sinking fund bonds, although with the improved system of financial administration this would not now be necessary, as serial bonds are used as the more advanced method of handling municipal indebtedness. Money is lost by keeping large amounts on hand uninvested. Again the tax burden may be greatly reduced through preventing this by properly estimating the year's needs and making adequate appropriations for them through a budget, as the law demands.

BONDED INDEBTEDNESS

All but ten of the towns reported uncollected taxes for the year in amounts varying from a few hundred dollars up to $40,000—most of them ranging, however, from $5,000 to $10,000. This is also evidence of poor business administration, but is, however, no more characteristic of the towns than of the counties or the larger cities in the state, as three of the latter reported over $100,000 uncollected taxes for the same year, which makes a very bad showing for municipal administration in North Carolina.

As to tax rates, we find great variation, which indicates individuality among municipalities as among individual citizens. Twelve of the towns had a general property tax rate of less than $1.00—two mill towns reporting 10 cents and one mill, respectively, the latter evidently being a mere camouflage for local self-government, while the town, as in many such instances, is really governed by a paternalistic mill control. All the other towns had a property tax of $1.00 or over, 11 of them paying a rate of $2.00 or more, which is allowed by law for the purpose of paying bonded indebtedness, though the limitation for general purposes (current expenses) is $1.00 per $100 valuation of property. (Municipal Finance Act.) In no case did the cities mentioned have a property tax exceeding $1.50, which is perhaps the point at which the greatest differentiation between city and town government occurs, as the presence of large corporations in the city relieves the individual taxpayer from paying such excessive rates. This, of course, is one of the arguments in favor of the larger unit of city government. As noted above, although the per capita cost of government may be more in the city than in the town, it is not usually the individual who pays, but the larger manufacturing industries and corporation interests. As to poll taxes, only 17, or about one-fourth, of the total number of towns have as low a rate as $1.00, although a constitutional amendment of 1917 made this the maximum limitation of the poll tax. However, this may be explained by the fact that these rates were levied for debts incurred prior to the date of the amendment, in which case they would be allowed to stand until the debts were liquidated. But we have no way of finding out in just how many cases this is true, or whether or not it is a deliberate or unintentional violation of the law, as there is no centralized state supervision of municipal administration nor any method of assurance that the legislative law will be enforced. Eight of these towns paid a poll tax of between $1.00 and $2.00; 14 between $2.00 and $3.00; and 17 had a poll tax rate of over $3.00, 5 of them paying as much as $5.00 and $6.00.

The large bonded indebtedness of the towns is one of their characteristic and most significant features, which constitutes, perhaps, their most serious problem. Only six towns report no bonded indebtedness, which, of course, does not necessarily mean that the town was well administered financially, but merely that it was unprogressive or had no public spirit for local improvements. Therefore, it is hard to interpret figures without knowing the individual towns themselves. Twelve of the towns had a bonded indebtedness of less than $100,000, while the remaining 47 reported a bonded indebtedness of from $100,000 to $600,000. The average for the group is about $200,000, while that of the cities is nearly twice as much in proportion to population. But again this must be thought of in terms of advantages received. The law on this point, as noted above, requires that the net debt shall not exceed eight per cent of the assessed valuation, except for certain purposes. The bonded indebtedness of one town exceeded 32 per cent of its assessed valuation, which may have been made legal through special enactment, but which appears to be an abnormally large proportion of its assessed valuation to be considered a wise financial policy. At any rate, such heavy bonded indebtedness is a challenge to study and investigation and the seeking of remedies for liquidation. Most of the towns reported some current liabilities, or short-term indebtedness for current expenses, which is permissible by law, but two of the towns reported over $100,000 in this column, which seems an unjustifiable amount for this item.

As to sinking funds, as discussed above, these are ceasing to be an important item of finance, since serial bonds are becoming more universal; only about two-thirds of the towns reported under this head, and most of them for small amounts, only one reporting over $100,000. The majority of the others were for amounts of less than $10,000.

CONCLUSIONS AND SUGGESTIONS

In view of the above facts, what are the next steps to be taken toward the improvement of municipal administration in North Carolina? Following are some of the things that might aid in this direction:

1. The assessment of all property at its actual or real market value, and the discovery of some method whereby a larger percentage of personalty would be listed. This would increase the revenue without any increase in the tax rate.

2. The discovery of whether or not public utilities owned by the towns really pay or whether it is more advisable to allow these services to be furnished by private companies, and the pursuit of a policy in accordance therewith. If the latter alternative is chosen, there should be some coöperative organization of municipalities whereby special wholesale rates for such services might be secured.

3. Some provision whereby the expense of public improvements, such as streets, which constitute such a heavy burden on the cities and towns, might be borne by others than the individual citizens. This might be done by diverting a part of the automobile or gasoline tax to this fund, or it might be shared by the county, if not by the state.

4. The practice of following a proper budgeting procedure, so that current liabilities might be lessened and expenses kept within income. Although this is now required by law, it is not always carried out. This should also prevent the holding of large sums of money in the treasury idle or uninvested.

5. Some system of administration whereby the collection of taxes might be enforced by holding the tax official liable. Some suggestions for procedure along this line might be had from the new county government law, which attempts somewhat the same thing for the county.

6. The discovery of other sources of revenue, so that such a large percentage of receipts from bonds or borrowed money will not be necessary. Various suggestions have been made recently as to new sources of revenue, some of which might very aptly be applied to municipalities.

7. Finally, less legislative control with its endless special legislation, and the granting of more freedom to the cities and towns. For the former system there should be substituted a state supervisory administrative control through some sort of municipal board, which would have the ability to advise as to policy and the power and authority to enforce the general municipal laws of the state and to see that they are not violated as at present. Such a board would be the means of obtaining the above-named steps. Such a board exists at present in name, but it should be made a vital part of municipal administration in North Carolina.

CONSUMPTION EXCISE TAXES FOR STATE PURPOSES

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Introduction

In recent years various schemes of taxation have been proposed to meet the increasing and expanding functions of state government. Along with several modifications of the general property tax, there have arisen the inheritance tax, the income tax, special taxes on corporations, the automobile license tax, the severance tax, and sales taxes of different kinds. All of these are of intense interest and significance. But this study will be confined to consumption excises on special or selected commodities.

Consumption excises or special commodity sales taxes are to be construed as "those taxes levied on the producer, manufacturer, wholesaler, retailer or other middlemen which it is the intention of the enacting body shall be passed on to the final consumer of the article taxed."[1] Specifically the taxes to be considered as coming under this classification are those levied upon cigars, cigarettes, and other tobacco products; admissions; soft drinks of all kinds; chewing gum; candy of a certain price; cosmetics; ammunition; and sporting goods. It is clear that the commodities embraced in this suggested list could not be classed as luxuries. Nor can they be classed as necessities. They may be better classed as non-essentials.

Because of its almost universal use by all the states, its general acceptance by students of public finance, and the special purpose for which it is levied, the consumption tax on gasoline will not be included in this study.

History

State consumption excises were used by several of the colonies before the establishment of the present federal government, and some few states levied excises on alcoholic beverages under state supervision of the whiskey traffic. However, it is only in recent years that we have had a clear development of this method of raising state revenue. It seems to have been a tradition or an unwritten law that consumption excises were to be reserved for the federal government. Certainly this was the practice from the Civil War until 1920. As late as 1917 the preliminary report of the committee appointed by the National Tax Association to prepare a plan of a model system of state and local taxation contained this statement: "In the course of its deliberations, the committee has had occasion to consider whether in view of the great increase in state and local expenditure in recent times, and the entrance of the federal government into the field of direct taxation which had hitherto been utilized by the states, it might be possible for the states to derive more revenue than in the past from taxes levied upon consumption. The taxes now levied by the states upon automobiles represent the sort of taxes the committee has in mind. Taxes on amusements, on non-alcoholic as well as alcoholic

[1]Miller, E. T., "State Excise Taxes," *Proceedings National Tax Association*, 1926. p. 225.

beverages, on hunting licenses, and a few other things have been brought to our attention; but we have decided to make no recommendation on the subject at this time. It is perfectly evident, that with the exception of automobiles, none of the taxes which have been suggested will ever be likely to constitute an important source of revenue, and we have preferred to concentrate attention this year upon the problems of chief practical importance."[2]

In South Carolina, where consumption excises have experienced a fuller development than in any other state in the nation, a special legislative report on revenue and taxation submitted to the General Assembly of 1921 states that "in the judgment of the committee no emergency of sufficient gravity now exists to warrant the state in embarking upon a venture of enacting a schedule of consumption taxes. In the absence of a settled conviction that such taxes should be made a permanent feature of our tax system, the committee feels that a resort to this form of taxation as a temporary expedient or for stop-gap revenues would not be justified."[3] Further, as recent as 1921, the *Bulletin of the National Tax Association* contained an address by an able economist in which it was stated that "taxation of consumption has in America generally been left to the federal government where there is good reason to believe that it will remain. It need not be further considered in a discussion of state and local taxation."[4]

This same attitude is usually taken by textbook writers, teachers, students of taxation, and public officials. They either ignore or pass over with a few general remarks the subject of state consumption excises. A rather careful survey of the published material shows relatively little attention given to this phase of state tax systems.

But in spite of this adverse position, forty-six states have entered the field in the case of the tax on gasoline, and no less than twelve have imposed excises on other commodities. Oregon was the first state to levy the tax on gasoline, February 25, 1919.[5] Since then the tax has been enacted in every state in the nation with the exception of New York and New Jersey.[6] The total amount collected from this one source during the year 1926 was $187,603,231.[7] The states which have levied consumption excises on commodities other than gasoline are Arkansas, Alabama, Connecticut, Georgia, Iowa, Kansas, Louisiana, North Dakota, Oregon, South Carolina, South Dakota, Tennessee, and Utah.[8] The field was entered first in 1921 by Connecticut with a tax on admissions, and Iowa with a tax on cigarettes. Then, in 1923, followed Georgia and South Dakota with cigarettes, Utah with tobacco in its

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[2]Bullock, C. J., and others, *Preliminary Report of the Committee Appointed by the National Tax Association to Prepare a Model System of State and Local Taxation*, 1918.

[3]South Carolina, *Report of Joint Special Committee on Revenue and Taxation Appointed by General Assembly of 1920*. p. 109.

[4]Fairchild, F. R., "The Future of State and Local Taxation," *Bulletin of National Tax Association*, VII, 3, p. 75.

[5]Klein, R. A., *American Highways*, V, 1.

[6]Gasoline tax of Illinois declared unconstitutional by state supreme court, February 24, 1928. Chi. Motor Club *v.* Kinney, 328 Ill.—160 N.E. 163. Ass. Press Dis.

[7]*Facts and Figures of the Automobile Industry*, 1927, p. 31. National Automobile Chamber of Commerce, Chicago.

[8]See Exhibit A in Appendix for details.

various forms, and South Carolina with cigars, cigarettes, ammunitions, candy, and admissions. Arkansas, with cigars and cigarettes, was the only addition in 1924. But in 1925 North Dakota imposed the tax on cigarettes, Oregon and Tennessee on all tobacco products, and South Carolina expanded her excises to embrace soft drinks of all kinds, ice cream, cosmetics, chewing tobacco, and snuff. Louisiana, with tobacco products, was the only state to enter in 1926. In 1927 Alabama and Kansas joined the ranks with cigarettes, and South Carolina made further expansion by taxing cut glass, playing cards, and sporting goods. From the information available Connecticut seems to be the only state to have withdrawn from the field after having once entered it. With the single exception of South Carolina, no state now taxes any commodities other than tobacco products.

A study of the rates imposed shows considerable uniformity among the states. While some levy the tax on the specific basis and others on the ad valorem, the actual amount of revenue realized per unit is approximately the same. The information on the cost of collection is not complete, but the data secured do not show that this item is disproportionately high. Six of the states specify that the revenue realized shall go into the general state fund, while six specify a particular purpose, usually education. It was noted that in practically every state which has had the excises for two or more years the original measure has undergone considerable revision and refinement to meet practical situations.

Clearly South Carolina has carried the consumption excises farther than any other state, and a more comprehensive survey of the situation there should prove of interest. The 1923 General Assembly imposed the tax on cigars, cigarettes, smoking tobacco, candy, ammunitions, and admissions. The rate on cigars ranged from $2.00 to $10.00 per 1,000; on cigarettes, $1.00 to $2.41 per 1,000; on smoking tobacco, 6 cents per pound; on ammunition, $2.00 per 1,000 rounds; on candy retailing for 80 cents or more per pound, 10 per cent; on admissions, 10 per cent. In all cases, except admissions, the tax was to be collected by the use of the adhesive stamp.[9] Due to the fact that similar stamps were used for a tax on bonds, notes and mortgages, and other legal documents, no exact estimate of the revenue derived from the consumption excises that year can be given. However, the total stamp tax for the nine months of the year (tax effective April 1) was $747,559, while the tax on admissions amounted to only $36,867.[10] The rates were so fixed that fractional stamps were necessary. This caused considerable annoyance, and necessitated increasing the price of the articles affected by a fractional cent more than the amount of the tax. Hence the 1924 general assembly changed the rates so as to eliminate this objectional feature.[11] The yield from the sales taxes for the year was $840,455; from the admission tax, $151,017.[12]

In 1925 the general assembly, against strong opposition, extended the consumption excises to include all soft drinks, ice cream, cosmetics, chewing

[9] *Acts of South Carolina.* No. 11, 1923.
[10] *Report of South Carolina Tax Commission,* 1923.
[11] *Acts of South Carolina,* No. 733, 1924.
[12] *Report of South Carolina Tax Com.,* 1924.

tobacco, and snuff. The tax on fountain drinks was 20 per cent; on bottle drinks, 1 cent for each 5 cents or fractional part thereof of the retail price; on cosmetics, 20 per cent; on chewing tobacco and snuff, 1 cent for each 3 ounces.[13] The measure was enacted as a section of the General Appropriation Act, thus making it operate for one year only. The fact is that it was accepted only as an emergency tax measure. The revenue derived from all the consumption excises for the year 1925 was as follows: tobacco, cosmetics, and candy, $1,090,698; admissions, $199,439; fountain drinks, including ice cream, $190,974; bottle drinks, $689,288. This makes a total of $2,170,399,[14] an amount which exceeded by nearly $700,000 the combined appropriations for the five institutions of higher learning.[15]

In 1926 the soft drink tax was reënacted as a part of the General Appropriation Act. But the excise on milk drinks, ice cream, and cosmetics was dropped.[16] The repeal of the former was largely the result of the conviction that the tax was hurting the dairy business; of the latter, the major factor was the evasion of the tax by the importation of articles from out of the state. However, the amount of revenue realized from the schedule of commodity excises for the year was not greatly reduced. The amounts collected were as follows: tobacco and candy, $937,203; admissions, $197,473; fountain drinks $121,172; and bottle drinks, $778,771; a total of $2,136,619.[17]

In 1927 all the consumption excise laws were rewritten as one revenue measure. The tax on tobacco was increased approximately 50 per cent, on ammunition 100 per cent, while a levy of 10 per cent was imposed upon playing cards, cut glass goods, and sporting paraphernalia. The tax on soft drinks was not changed.[18] The very fact that these measures were enacted independent of the General Appropriation Act seems to indicate that they are being accepted as a permanent feature of the state tax system.

The only development thus far in 1928 is the passage of a measure designed to tighten up the collection of the tax on soft drinks.[19]

One would judge from the steady growth of the commodity excises in South Carolina that they have not been vigorously opposed. Such is far from the real situation. None of these measures was passed without a bitter fight, and then only by a narrow margin. This is particularly true of the tax on soft drinks. During the summer of 1925 the bottlers and druggists organized what was wrongly styled the Citizens Coöperative Tax Association for the purpose of fighting the tax. They carried on a vigorous campaign through the newspapers in the form of full- and half-page advertisements which contained numerous misstatements. Needless to say, they exerted all possible pressure on members of the general assembly. And in this they were considerably aided by a well-known corporation of an adjoining state. Further, in the primary

[13] *Acts of South Carolina*, No. 197, Sec. 82. 1925.
[14] *Report of South Carolina Tax Com.*, 1925.
[15] *Acts of South Carolina*, No. 197, 1925.
[16] *Acts of South Carolina*, No. 475, 1926.
[17] *Report of South Carolina Tax Com.*, 1926.
[18] *Acts of South Carolina*, No. 73, 1927.
[19] *The State*, Columbia, S. C., March 7, 1928.

election of 1926 they confessedly had their own man for governor and their own candidates for membership in the legislature. Some rather startling tactics practiced by the organization were uncovered by one of the leading newspapers of the state. There are many who believe that these measures defeated their own purpose.

However, it is safe to say that had not the state been faced with an increasing cost of state government and a disastrous shrinkage in the value of farm crops, this form of taxation would not have been instituted. In other words, the consumption excises were enacted to relieve the tax burden on farm property.

THE CASE FOR CONSUMPTION EXCISES

But what are the arguments in favor of state consumption excises? Upon what grounds can those states which have imposed a sales tax upon special commodities justify their action?

From a necessarily limited survey the conclusion is reached that the matter of abstract theories and principles of taxation has been of relatively little moment in the framing of such tax measures. They have been enacted largely by reason of the fact that they produced needed revenue. It has been a matter of necessity, either fancied or real. Of recent years the various state governments have been faced with rising governmental costs and relatively declining revenue from tangible property, the usual source of supply. To meet this deficit, new sources had to be tapped or the burden increased on land and improvements. The former course was chosen, and in the movement the sales tax on special commodities was included. The tax commissioner of Connecticut states in his report for 1921-1922 that the tax on admissions in that state "demonstrates the feasibility of securing additional revenues from other sources rather than imposing further taxation on real estate."[20] The South Dakota Tax Commission in its 1924 report said, in reference to the gasoline and cigarette tax, that "this form of taxation so far inaugurated in this state is proving entirely satisfactory in that it tends to shift the burden of taxation from tangible property."[21]

The fact that all of the states that have resorted to this form of taxation are predominantly agricultural states in which land bears the burden of the general property tax is indicative that this position has generally prevailed. It clearly did in South Carolina. Since 1921 there has been the firm conviction —reasoned or unreasoned—among practically all classes that relief must be given tangible property, and particularly farm lands. So strong has been the sentiment that it caused the rather impetuous chairman of the ways and means committee, who led the fight for the tax on soft drinks, to say on the floor of the lower house that he would hold the legislature in session "until hell freezes over" before he would consent to a raise in the levy on tangible property. And relief was given. The levy was reduced from 12 to 5 mills.

Whether or not this position has been justifiable may be a debatable point. But without doubt in some states tangible property has been unduly

[20]Quoted by Miller, E. T. "State Excise Tax," *Proceedings National Tax Association*. 1926.
[21]*Ibid.*

burdened, has been forced to pay more taxes than the returns from the property justified. This was particularly true of farm lands after the deflation of 1920-21. Even a casual study of the census data covering the states which have imposed the consumption excises reveals a tremendous shrinkage both in the value of farm property and in the worth of annual products. To bear increasing tax burdens under such conditions was obviously a hardship—in some instances, an impossibility.

Several distinct arguments, other than the matter of necessity, have been advanced for consumption excises. It has been maintained, and with considerable justice, that they reach a class of people who otherwise pay no taxes. Under the property and income system only those who possess property or enjoy an income above a certain amount contribute to the support of the government. Consequently only a small proportion of the citizens bear the burden. Large numbers of wage and salary earners, men without families, clerks, sports, and others escape. A tax on commodities of wide use and of inelastic demand would reach this group, and thus distribute the burden of taxation. The 1925 report of the South Carolina Tax Commission expresses the opinion that "on account of the so-called indirect taxes, a greater percentage of the citizens of our State are contributing to the cost of State Government than any other State in the United States."[22]

This position is clear. There are relatively few who are not consumers of either tobacco products or soft drinks. It is also clear that in a democracy the matter of civic alertness and responsibility makes it desirable that a large proportion of all citizens contribute to the support of the government. But it is not clear that this condition is not obtained under property and business taxation. There are those who hold that these taxes are shifted to the ultimate consumer. Of this more will be said in the following section of this study.

Further, it is held that no one is compelled to pay the tax, since the commodities on which the excises are imposed are not necessities. If the individual is adverse to paying the 10 per cent levy on candy which retails for 80 cents or more per pound, he can escape by not buying candy or by buying a cheaper quality. Similarly, if he does not choose to pay the tax on tobacco, he can simply refrain from smoking, chewing, and dipping. The laws, customs, and standards of living of modern society do not force him to use these commodities. They are not essential to the maintenance of health. They are not even prerequisites to one's social position. This is not true of tangible property. An individual must have a home, or a house in which to live. Society must cultivate land to supply the raw materials. Factories must be built to manufacture clothes and to process food. Stores, banks, and railroads must be organized to bring food and clothing from the field of production to the point of consumption. These are properties without which the individual can not exist in modern society. A tax on these is a tax on necessities. The levy must be paid, or the property is confiscated.

This attitude has been of considerable weight in the states which have imposed the consumption excises. It has been particularly strong in South

[22] *Report of South Carolina Tax Com.*, 1925, p. 13.

Carolina. In both branches of the general assembly and in the press of the state the assertion was frequently made that the consumption excise was a tax that the sheriff would not be called upon to collect (referring to the situation that a considerable number of sales had to be executed by the sheriffs to collect the property tax). The fact is that sales have not been executed to the extent that the actual conditions warrant. Delinquent property taxes since 1921 have run into the millions of dollars, and no one has as yet had the courage to enforce their collection.

Related to the above position is the idea that the tax is paid unconsciously. Since it is paid in small portions throughout the year, the taxpayer does not feel the burden as keenly as he does the tax on property and income, which is payable annually or semi-annually. He is therefore less disposed to grumble. It is what may be termed "painless extraction."

It is doubtful if this is true of all the excise taxes now in force. It is perhaps true of the gasoline tax to a larger extent than any of the others. Few motorists are conscious that they are paying a 10 to 20 per cent consumption tax when they purchase gasoline. It is much less true of the tax on tobacco products and soft drinks. In the case of gasoline, the price per gallon has not been standardized. It may retail for 16 cents this week and for 18 cents next. As a result, the consumer has not formed the habit of expecting to pay a definite amount per gallon. Moreover, the price per gallon does not usually run in a figure of which five is a multiple, as 10, 15 or 20 cents. It has become habitual to expect the price to be expressed in odd cents, as 17, 18, 19, or 21. Thus a tax of 2, 3, or 4 cents per gallon is not readily noticeable. In the case of tobacco products, the situation is different. The purchaser of these commodities has become accustomed to paying a definite price per unit. This price is almost invariably a figure of which five is a multiple. The consumer has acquired the habit of paying 10, 15, or 20 cents for his package of cigarettes or smoking tobacco; 5 or 10 cents for his cigars; and 5 cents for his coca cola. Thus an addition of a few cents to the regular price is immediately noticed. Instead of giving the dealer 15 cents for his package of cigarettes or smoking tobacco, he is compelled to give him 20 cents and receive 2 or 3 pennies in change; or instead of giving a nickel for his soft drink, he gives a dime and receives four pennies in change. Under these circumstances it is obvious that the few cents tax is not paid unconsciously.

The point is made that these odd-cent charges could be eliminated and the tax thus made unnoticeable by simply reducing the number of cigarettes in a package, or the ounces of tobacco in a can, or the size of the soft drink commonly sold. This is hardly practicable, since the manufacturers of these commodities do not confine their sales to any particular state. The tax is not imposed by all states and the rates are not uniform in those states in which it is imposed. Clearly, producers could not make packages to fit the different tax systems. Moreover, retail dealers have not shown a disposition to want this thing done, since the success of their efforts to have these taxes repealed is largely dependent on making them unpopular with consumers.

Further, students advance the idea that it is expedient in the interest of safety to have a balance between direct and indirect taxes,[23] and that the commodity excises provide this balance to a system which is now in the main direct.[24] Direct taxes are held to be relatively inelastic. The consumption excise is elastic and can be so changed and added to as to respond to the changing needs of the government for revenue. This has been the development in South Carolina. As the need for more revenue arose, more commodities were taxed and the rate increased on those already bearing the levy. Such a procedure has enabled the state to carry on activities which it otherwise could not have done.

But there are limits to this scheme. The commodities upon which a state can levy a consumption tax with any degree of fairness and success are confined to a relatively small number. And there are limits to the rates imposed beyond which the state can not go. As a practical matter, if the state sought to impose the tax so as to embrace a larger number of commodities, or imposed heavy rates, it is reasonable to think that the citizens would reduce their consumption of the goods taxed, and thus defeat the purpose of the tax scheme. When this condition is reached, then the indirect (consumption excises) system is no more elastic than the direct.

From an administrative standpoint it is held that the consumption excise has the advantage of being easily and inexpensively collected. This is particularly true of those commodities on which the tax can be collected by the use of the adhesive stamp.

Some difficulty in enforcing the scheme is almost inevitable. Some evasion has occurred. But considering the recentness of consumption excises in state tax systems and the consequent lack of a developed technique of administration, the difficulty in enforcement is not greater than in other tax measures. In Tennessee it is estimated that the actual collection is 79 per cent of the potential,[25] and in South Carolina the tax commission reports that "there have been wilful evasions of the law in some instances, but we feel that these are not more numerous than might be reasonably expected."[26]

The cost of collection is not easily determined. But estimates by the various states show that it is relatively reasonable. In Tennessee the cost is limited by statute to 2 per cent.[27] In Arkansas the cost is given as 2.3 per cent;[28] in Georgia, it is 3.5 per cent;[29] in Iowa, it is from 5 to 6 per cent;[30] in South Carolina it is "slighthly less than 3 per cent."[31]

One of the strongest arguments advanced is that the excise is more or less regulatory of the consumption of the commodities taxed. The wide and great use of these articles is held to be of no benefit, and, in many cases, of positive

[23]Sherras, G. F., *The Science of Public Finance*, ch. XXV. The Macmillan Co., 1924.
[24]Ely, R. T., *Outlines of Economics*, ch. XXXIV. The Macmillan Co., 1923.
[25]Miller, E. T., *op. cit.*, p. 231.
[26]*Report of South Carolina Tax Com.*, 1924.
[27]Miller, E. T., *op. cit.*
[28]Letter from Arkansas Department of Revenue, Feb., 3, 1928.
[29]Miller, E. T., *op. cit.*
[30]*Ibid.*
[31]Letter from W. G. Query, Chairman South Carolina Tax Com., Feb., 29, 1928.

harm to personal health and social welfare. Hence the consumption ought to be checked by imposing a tax. Undoubtedly this was an underlying motive in some states that have levied the tax on cigarettes. Several of them were among the states that formerly had laws forbidding the sale of cigarettes to minors.

Whether, in fact, the operation of the tax has regulated consumption is difficult to determine. If the tobacco and soft drink manufacturers and dealers are right in contending that the tax has placed a heavy burden upon them in that it has lowered the consumption of the goods upon which their business depends, then the desired end is being accomplished. In one large cotton mill of South Carolina it is reported that since the imposition of the tax on soft drinks, the operatives drink milk instead of soft drinks with their lunch. If this be true, there is a decided gain. But whether this condition has been brought about by the tax, or the efforts of educational and health forces, or the need for a bigger market for the milk from the dairy owned and operated by the mill company, is a question that this study will not attempt to answer. However, there is some evidence in the annual figures of the bottling industry of South Carolina that the tax has reduced the consumption of soft drinks. These figures will be given in the following section.

THE CASE AGAINST THE TAX

The principal argument offered against the consumption excise is that it is not taxation according to ability to pay, that it is in effect a regressive tax. Admittedly, this would be true if the tax were levied on necessities or essentials, such as foodstuffs and clothing. But the position can hardly be maintained as regards the tax on soft drinks, candy of a high grade, tobacco products, and admissions. It is not reasonable to believe that the poorer classes spend a greater proportion of their income for these than do the middle and upper classes. And if they do, they are doing it voluntarily and possibly at the sacrifice of the necessities of life. If they spend considerable sums for these non-essentials, this very fact is fair evidence of taxpaying ability.

Then the position is taken that while the commodities affected are not necessities, they are also not luxuries. They are classed rather as enjoyments. And it is held that "taxes should not prohibit or even restrict harmless pleasure, and the fact that there are reckless joy riders, and tobacco fiends should not lead to penalizing by high taxes the more conservative of these consumers."[32]

To apply this idea to the systems of taxation now generally in operation would condemn nearly every phase of them, and little revenue could be raised for the support of governmental activities. A person ought not be restricted in his desire to own a home and yet the property tax, in its actual operation, does that very thing. A tax ought not penalize thrift and energy and yet a tax is imposed on incomes. The fact is that when we tax a man's home or his savings, we are taxing necessities in a very real sense. But when we tax his

[32]Miller, E. T., *op. cit.*, p. 231.

soft drinks and tobacco we are touching merely his enjoyments. It seems that this position is almost wholly untenable.

A further objection is raised by those who hold the theory that the men of the streets—the masses, so to speak—bear shifted property and business taxes. It is maintained that it is not necessary to impose a consumption excise to reach all classes. They are already reached by tax diffusion.

But, as a matter of fact, it is by no means certain that property and business taxes are shifted to the ultimate consumers. The whole matter of the shifting and incidence of taxation is in a controversial stage. It is generally assumed that the tax on improvements is shifted to the users, but even here a great deal depends upon the state of development of the community in which the improvements are located—whether it is in a progressive, stable, or declining state. A tax on land is regarded as not capable of being shifted. A tax on business may or may not be shifted, depending upon the matter of monopoly, the conditions of the cost of production, the nature of the business, and other factors of varying importance. Certainly, no definite conclusion can be reached that this position is valid.

But, granting that property and business taxes are shifted to the ultimate consumers, the question arises as to whether or not it is better to impose the tax by a method in which it is certain that they will pay than in a way in which there is considerable uncertainty.

The objection that the cost of collection is high is not substantiated by the facts. This phase was covered in the preceding section.

Another argument brought against the consumption excise is that it increases the price of the commodity by more than the amount of the tax. This, too, is not substantiated by the facts. So far as can be determined from the information available, this condition does not prevail for any of the articles in any of the states. It did exist in South Carolina during the first year of operation of the cigarette tax when the rates imposed were such that fractional stamps were necessitated. After this objectional feature was eliminated the practice ceased.

However, it can not be denied that if the tax is levied at the point of production, there would be a tendency for this condition. The wholesalers, jobbers, and retailers would seek to secure profits not only on the money they invested in the commodity itself, but also on the outlay for the tax which is passed successively down to them.

Of possibly more weight is the contention that the tax is difficult to enforce on a state-wide basis; that it is generally evaded by bootlegging and substitution. Undoubtedly, this danger always exists, and can be avoided only by a careful selection of articles and the framing of definite and reasonable tax measures. The states that have the tax have experienced some difficulties. Georgia reports the amount of evasion as "considerable."[33] Tennessee estimates that 21 per cent of the potential is uncollected.[34] In South Carolina a number of difficulties have arisen. When the 20 per cent cosmetic tax was imposed, the

[33]Miller, E. T., *op. cit.*, p. 231.
[34]*Ibid.*

drug and department stores across the state line reported a considerable increase in the sale of these articles to South Carolina consumers. The condition was such that the tax was repealed after one year of operation. Again, in 1925, when the 20 per cent tax on ice cream made the 5-cent cone retail for 6 cents retailers reported a tremendous increase in the sale of 5-cent packages of candy and a corresponding decrease in the sale of ice cream in the cone. Whether there is much evasion of the tobacco and soft drink tax is almost impossible to determine with any degree of accuracy. As regards bottle drinks, the bulk and weight in proportion to value are so great that the cost of transportation from other areas by the individual consumers would be greater than the tax. In the case of tobacco, North Carolina concerns have occasionally placed advertisements in South Carolina newspapers offering attractive prices, but this has been practiced so seldom that one is forced to believe that the business has not been large.

There has been evasion other than through importation and substitution. It is difficult to evade a tax on goods which are so packaged as to permit the use of adhesive stamps. But on those goods where this is not readily possible, the tax is not easily collected. South Carolina has had this difficulty with admissions and soft drinks, the tax on which is collected without the use of stamps. The State Tax Commission estimates a loss of nearly $300,000 annually by the failure of dealers to remit all the revenue due the state.[35] The situation has led the tax officials to recommend, and the general assembly to enact into law, the provision that theater tickets be either official or bear the stamp of the state, that bottle drinks bear durable paper stamps firmly affixed or stamped crown caps, and that the containers of syrup used in compounding fountain drinks be stamped at the time of opening.[36] It is reasonable to believe that this will make the tax more effective.

One of the effective arguments used against the consumption excise taxes is that they reduce the consumption of the articles taxed and thus hurt the business of the manufacturers of these commodities who have invested capital in perfectly legitimate enterprises. Just how much, if any, has been the decrease in consumption as a result of the tax would be very difficult to ascertain, and would entail more research than can be done in this study. Since the commodities concerned are those in which the demand is rather inelastic, it is reasonable to assume that it has been relatively small. However, an effort was made to check up on the claim of the South Carolina bottlers that their business had been hurt by the soft drink tax. The compilation below gives the main facts about the industry for the two years before the tax (1923 and 1924) and for the three years (1925, 1926, and 1927) after the tax was imposed.[37]

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[35] *The State*, Columbia, S. C., March 2, 1928.

[36] *Ibid.*

[37] Compiled from the annual reports of the South Carolina Department of Agriculture, Commerce, and Industries for the years 1923, 1924, 1925, 1926, and 1927.

Year	*No. of Plants*	*Capital Invested*	*Value of Annual Product*
1923	103	$1,369,076	$2,315,590
1924	97	1,563,247	2,996,684
1925	88	1,496,469	2,836,009
1926	78	1,314,231	2,649,404
1927	—	1,293,583	2,704,423

As regards all three items—number of plants, the capital invested, and the value of the annual products—there has been a loss. This condition in the face of an increase in the business of manufacturing generally in the state seems to indicate that the claim of the bottlers is correct. But these figures may not be altogether reliable. They are furnished the State Department of Agriculture, Commerce, and Industries by the bottlers themselves, and it is to their interest to make as poor a showing as possible in order to get the tax repealed.

Another objection is that the tax and its enforcement are harassing to the dealers. This has perhaps been the greatest cause of complaint in South Carolina, and has won for all the state excises the title of "nuisance taxes." Dealers constantly complain that the agents sent out by the State Tax Commission are dictatorial, arrogant, and otherwise annoying. The collection of the excises in pennies involves vexatious details against which they protest vigorously. And not a few object to acting in the capacity of tax collector for the state without remuneration. However, this attitude is not as strong now as it was at the beginning of the operation of the tax—due, no doubt, to increased efficiency of administration and a wider acceptance of the tax by all concerned. Let it be said, however, that there has never been much voiced opposition on the part of consumers.

A final objection urged is that the tax on special commodities is unconstitutional in that it is class legislation. The South Carolina bottlers have constantly threatened to carry the soft drink tax to the courts to subject it to the test, but they have not yet done so. There seems to be little weight to the claim since the courts have generally upheld the tax on gasoline.[38] There has been only one exception. The supreme court of Illinois recently declared the 2 cents per gallon tax on gasoline of that state unconstitutional.[39] This was due probably to a technical defect in the law rather than the result of any conflict of principles.

Principles of Consumption Excises

From a survey of state consumption excises as they now exist, a consideration of the arguments both for and against this scheme of raising revenue, and a study of the general principles of taxation, certain conclusions are reached as to the principles which ought to obtain in this form of taxation.

1. The commodities affected should be those that are not characteristically within the subsistence level. Only those which may be classed as luxuries or

[38] *The Gasoline Tax.* A Special Report of Joint Committee on Taxation and Retrenchment, New York.

[39] Associated Press Dispatch, February 24. 1928.

non-essentials could escape forcing a regressive tax both in theory and practice. Obviously, an excise on sugar, flour, coffee, fruit, meat, and milk would impose a heavier burden upon the poor than upon the rich; while a tax on soft drinks, tobacco, and high-priced candy would not possess this defect to any marked degree.

2. The excise should be on those classes of goods, the consumption of which does not confer any particular benefit upon the consumer, and which are socially unnecessary or positively undesirable. Tobacco may or may not be harmful, but it would require considerable juggling of the reason to maintain that it is necessary, or that it confers any special benefit upon society.

3. The tax should be imposed as close as possible to the point of consumption. This is necessary to prevent the article taxed from retailing at an increase in price which is greater than the amount of the tax. For example, if an article is taxed at the point of production, and is of the kind which passes through the hands of a number of middlemen before reaching the final consumer, the increase in price will have a tendency to be greater than the amount of the tax by reason of the fact that the various middlemen will try to get a profit on not only the money invested in the article itself but also on the amount invested in the tax.

4. The tax should be placed only on those commodities that are widely used and that enjoy an inelastic demand. Unless this condition obtains little revenue will be realized, thus defeating one of the main justifications of the consumption excise.

5. As few articles as possible should be taxed. It is apparent that to spread the tax over a large number of commodities would increase the cost of collection and enforcement out of all proportion to the amount of revenue raised. There is some reason to believe that in South Carolina the number is now too large.

6. The rate should not be excessively high, lest evasion be practiced by bootlegging, substitution, and curtailment of consumption. This fault existed in the South Carolina 20 per cent tax on cosmetics, and the 1927 rate of $4.00 per 1,000 rounds on ammunition. Both were evaded.

7. The goods should be those which are so packaged that the tax can be collected by the use of the adhesive stamp. Otherwise there is a tendency for the dealer to retain the tax after it has been paid by the consumer. This has been the main defect of the soft drink and admission tax.

CONCLUSION

From an examination of the facts, ideas, and opinions presented in this study, the conclusion can not be escaped that as a means of financing all or a major part of the functions of state government, consumption excises will prove inadequate. South Carolina derives more revenue from this source than does any other state, and yet she secures from it less than 20 per cent of her annual appropriations.

But as a supplement to the sources now generally accepted—assuming that the principles set forth above obtain—little valid objection can be raised against this method of taxation. There is a lack of equity in the tax systems of almost all the states, and there is a real problem in how to secure equity and at the same time realize sufficient revenue to finance state activities. The measures usually advanced from which to choose are the income tax, corporation tax, the severance tax, the inheritance tax, and the modified property tax. May it not be reasonably concluded that the consumption excise tax possesses features which would clearly warrant including it in this group?

EXHIBIT A

CONSUMPTION EXCISES BY STATES

1	2	3	4	5	6
STATE	Date imposed[1]	Commodities	Rate	Annual yield[14]	Cost of Collecting Per cent
Alabama[2]	1927	Cigars and cigarettes	15% of wholesale price		
		Cigars	10% retail price	$1,044,000	2.3
Arkansas[3]	1925	Cigarettes	20% retail price		
Connecticut[4]	1921	Admissions	½ Federal tax	Repealed in 1924	
Georgia[5]	1923	Cigarettes	10% retail price	$ 800,000	3.5
Iowa[6]	1921	Cigarettes	1 to 2 mills per cigarette	$ 808,336	5 to 6
Kansas[7]	1927	Cigarettes	2 cents per 20 cigarettes		
Louisiana[8]	1926	Tobacco products	1 cent per 10 cents of retail price		
North Dakota[9]	1925	Cigarettes	1½ to 2 mills per cigarette	$ 237,496	
		Snuff	2 cents per 1¼ oz.		
Oregon[10]	1925	Tobacco	Graduated rate		
South Carolina[11]	1923	Cigars, cigarettes and smoking tobacco	1 cent[13] for each 5 cents of retail price	$ 936,203	
		Ammunition	$4 per 1,000 rounds		
		Candy	10% retail price		
		Admissions	10%	$ 197,473	Less than 3
	1925	Chewing tobacco and snuff	1 cent for each 3 oz.		
		Soft drinks, Ice cream[12], Cosmetics[12]	20% retail price	$ 999,943	
	1927	Cut glass goods, playing cards, sporting goods	10% retail price		
South Dakota[15]	1923	Cigarettes	1 to 4 mills per cigarette	$ 337,710	
Tennessee[16]	1925	Tobacco products	10% retail price	$1,229,607	2
Utah[17]	1923	Cigarettes	1 to 2 mills per cigarette	$ 130,000	

[1]Dates given in this column are those when the excises were first imposed. All other data in the table are the latest available.
[2]Alabama Revenue Bill of 1927, p. 4.
[3]Personal letter from State Department of Revenue, Feb. 3, 1928, and Cigarette and Cigar Law of Arkansas, Act 147, 1927.
[4]Miller, E. T., "State Excise Taxes," *Proceedings of National Tax Association*, 1926.
[5]*Ibid.*, and personal letter from Georgia State Tax Commission, February, 1928.
[6]Personal letter from State Treasurer, Feb. 23, 1928, and Iowa Cigarette and Tobacco Law, 1927.
[7]Personal letter from Kansas Public Service Commission, Feb. 28, 1928, and Kansas Cigarette Law, 1927.
[8]Personal letter from Louisiana Tax Commission, Feb. 3, 1928, and Louisiana Tobacco Law, Act 197, 1926.
[9]Personal letter from North Dakota Tax Commission, Feb. 6, 1928.
[10]Miller, E. T., *Op. cit.*
[11]Compiled from *Acts of South Carolina*, No. 73, 1923; No. 197, Sec. 82, 1925; No. 475, 1926; No. 73, 1927; *Report of State Tax Commission*, 1926; and personal letter from W. G. Query, Chairman of State Tax Commission, Feb. 29, 1928.
[12]Tax repealed in 1926.
[13]Rates as of 1927.
[14]Yield for 1926.
[15]Personal letter from South Dakota Department of Finance, Feb. 6, 1928, and South Dakota Law regulating the sale of cigarettes, 1925.
[16]Miller, E. T., *Op. cit.*
[17]Personal letter from Utah Attorney General, Feb. 6, 1928, and Utah statute taxing cigarettes, 1923.

EXHIBIT B

ESTIMATED YIELD OF REVENUE TO NORTH CAROLINA FROM VARIOUS COMMODITY EXCISES*

1. From cigars, cigarettes, smoking and chewing tobacco, snuff, ammunition, and candy	$1,506,440
2. Admissions	318,670
3. Soft drinks	1,593,350
	$3,418,416

*The above estimates were secured by getting the per capita yield of the various excises in South Carolina and then applying this figure to the population of North Carolina. All data are for the year 1926.

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